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ADVANCED CORPORATION LAW

A PRACTICAL APPROACH TO CORPORATE GOVERNANCE

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Chapter 3. Director Independence 1
A. State Law 1
D. Choosing Directors 1
California Corporations Code § 301.4 1
Notes and Questions on Board Diversity 2
Chapter 5. Operationalizing the Monitoring Model: Federal Law 4
Section A. Independent Auditors 4
Chapter 6. Executive Compensation 5
Section A. Introduction and Overview 5
Section D. Federal Law 8
Pay Versus Performance, Exchange Act Release No. 95,607 (August 25, 2022) 11
Chapter 8. Insider Trading 17
Section C. Compliance Programs 17
Chapter 9. Voting and Proxies 18
B. Federal Proxy Regulation 18
Universal Proxy, Exchange Act Release No. 93,596 (Nov. 17, 2021) 18
Note on Universal Proxy Card Forms 20
Chapter 11. Shareholder Activism by Proxy Contest 26
B. Historic Disincentives to Activism Via Proxy Contests 26
C. Defenses Against Proxy Contests 26
1. Basic Legal Standard 26
Coster v. UIP Companies, Inc., --- A.3d ---- (Del.2023) 26
Notes and questions 33
Chapter 12. Shareholder Activism via Proposals 37
A. Rule 14a–8 37
C. Management Resistance to Proposals: Grounds for Excluding a Proposal 38

Chapter 3. Director Independence

A. State Law

***Page 68.* Add new note 6.**

6. In *Sciabacucchi v. Liberty Broadband Corp.*,[1] Delaware Vice Chancellor Glasscock explained that the independence inquiry varies by context:

> Where the independence inquiry relates to special litigation committees, it requires a showing of independence by the special litigation committee, having displaced the common-law presumption of director independence. . . .
>
> The independence inquiry as it relates to demand futility arises in the context where the challenged directors are not themselves interested in the question posed in the demand, but are alleged not to be independent of those who are. Where the latter are fellow directors, the required demonstration appears to be the easiest for a plaintiff to clear, given the natural reluctance of directors to take the action demanded—ultimately, choosing to sue fellow directors. If . . . the difficulty of impartially assessing a demand to sue fellow board members (or to sue business associates, friends, family, etc.), is high, it follows that a plaintiff would find it easier to impugn a director's independence in the context of demand futility. Successfully impugning a director's independence with respect to voting on transactions, conversely, should be more difficult than challenging that same independence with respect to assessing a demand. The ultimate factual burden upon a plaintiff to prove a director's lack of independence at trial will vary accordingly. The important point is that the decision in question must be viewed in the context of the director's relationship and her ability, in light of that relationship, to apply her business judgment thereto. . . .
>
> "Delaware law does not contain bright-line tests for determining independence but instead engages in a case-by-case fact specific inquiry based on" the facts. Facts submitted to rebut the presumption of independence should be reviewed "holistically, because they can be additive." Plaintiffs seeking to show that a director was not independent must demonstrate that the director in question had ties to the "person whose proposal or actions he or she is evaluating;" ties so substantial that she could not "objectively discharge ... her fiduciary duties." The inquiry is whether those ties were material such that they displace the impartiality of the individual director.

D. Choosing Directors

***Page 108.* Insert the following above the heading "Questions."**

California Corporations Code § 301.4[2]

. . .

(b) No later than the close of the 2022 calendar year, a publicly held domestic or foreign corporation whose principal executive offices, according to the corporation's SEC 10-K form, are located in California shall comply with the following:

> (1) If its number of directors is nine or more, the corporation shall have a minimum of three directors from underrepresented communities.
>
> (2) If its number of directors is more than four but fewer than nine, the corporation shall have a minimum of two directors from underrepresented communities.

---

[1] CV 11418-VCG, 2022 WL 1301859 (Del. Ch. May 2, 2022).

[2] The full text of § 201.4 is reprinted in Appendix 2.

(3) If its number of directors is four or fewer, the corporation shall have a minimum of one director from an underrepresented community.

. . .

(d) (1) The Secretary of State may adopt regulations to implement this section. The Secretary of State may impose fines for violations of this section as follows:

(A) For failure to timely file board member information with the Secretary of State pursuant to a regulation adopted pursuant to this paragraph, the amount of one hundred thousand dollars ($100,000).

(B) For a first violation, as described in paragraph (2), the amount of one hundred thousand dollars ($100,000).

(C) For a second or subsequent violation, as described in paragraph (2), the amount of three hundred thousand dollars ($300,000).

(2) For the purposes of this subdivision, both of the following apply:

(A) Each director seat required by this section to be held by a director from an underrepresented community, which is not held by a director from an underrepresented community during at least a portion of a calendar year, shall count as a violation.

(B) A director from an underrepresented community having held a seat for at least a portion of the year shall not be a violation.

(3) Fines collected pursuant to this section shall be available, upon appropriation by the Legislature, for use by the Secretary of State to offset the cost of administering this section.

(e) For purposes of this section, the following definitions apply:

(1) "Director from an underrepresented community" means an individual who self-identifies as Black, African American, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian, or Alaska Native, or who self-identifies as gay, lesbian, bisexual, or transgender.

(2) "Publicly held corporation" means a corporation with outstanding shares listed on a major United States stock exchange.

***Page 108*. Delete questions 3 to 5 and replace with the following.**

3. How do §§ 301.3 and 301.4 apply to newly public companies that IPO late in a year (e.g., December 2025)?

4. Sections 301.3 and 301.4 both say there is no violation if a woman or member of an underrepresented community held a seat for at least a portion of the year, but how small is a portion?

5. What if there is a proxy contest, and the women or members of an underrepresented community nominated by the company lose?

***Page 112*. Delete the heading "Note and Questions" and the note and questions that follow. Insert the following in their place.**

Notes and Questions on Board Diversity

1. The Delaware Supreme Court has stated that:

> Corporations and individuals alike enter into contracts, commit torts, and deal in personal and real property. Choice of law decisions relating to such corporate activities are usually determined after consideration of the facts of each transaction. In such cases, the choice of law determination often turns on whether the corporation had sufficient contacts with the forum state, in relation to the act or transaction in question, to satisfy the constitutional requirements of due process. The internal affairs doctrine has no applicability in these situations. Rather, this doctrine governs the choice of law determinations involving

> matters peculiar to corporations, that is, those activities concerning the relationships *inter se* of the corporation, its directors, officers and shareholders.[3]

a. Is board diversity an internal corporate affair? Does it matter whether one is applying the internal affairs doctrine as a rule of conflicts of law or one of constitutional law?

b. Is electing directors an internal corporate affair?

c. Is filling board vacancies an internal corporate affair?

2. A number of lawsuits were filed challenging the constitutionality of §§ 301.3 and 301.4. In *Meland v. Weber*,[4] the Ninth Circuit held that a shareholder of publicly traded company with headquarters in California had standing to bring a § 1983 action alleging that § 301.3 discriminated on the basis of sex in violation of the Equal Protection Clause of the Fourteenth Amendment. As of this writing, the case remains pending before the District Court.

In *Crest v. Padilla*,[5] a Los Angeles Superior Court judge held that:

> Section 301.4 clearly applies suspect categories: it imposes a duty on corporations to use such categories in the selection of their board members. It requires corporations to have a specific number of directors who are members of certain listed races, or else have certain listed sexual orientations or gender identities. People of other races, orientations, and identities are necessarily excluded from those board seats.[6]

The court concluded:

> Because Section 301.4 treats similarly-situated individuals differently based on race, sexual orientation, and gender identity, because that use of suspect categories is not justified by any compelling interest, and because the statute is not narrowly tailored to serve the interests offered, Section 301.4 violates the Equal Protection Clause of the California Constitution. Plaintiffs are entitled to a judgment declaring as much and an injunction preventing the expenditure of taxpayer funds on implementation of the measure.[7]

A different Los Angeles Superior Court judge subsequently held that § 301.3 was unconstitutional on similar grounds:

> Judge Duffy-Lewis, following a three-month bench trial, found that the state failed to meet its burden to show that the proffered interests of improving the economy, corporate performance and governance, and opportunities for women in the workplace were sufficiently compelling to justify the statute's use of a suspect, gender-based classification as required by the Constitution's Equal Protection Clause.[8]

Neither decision addressed the internal affairs aspects of the legislation.

---

[3] McDermott Inc. v. Lewis, 531 A.2d 206, 214–15 (Del. 1987).

[4] 2 F.4th 838 (9th Cir. 2021).

[5] 2022 WL 1073294 (Cal.Super. 2022)

[6] Id. at *8.

[7] Id. at *20.

[8] Second California Law Mandating Specific Number of Underrepresented Directors Struck Down as Unconstitutional, Corp. Gov. Adv. 4134941.

CHAPTER 5. OPERATIONALIZING THE MONITORING MODEL: FEDERAL LAW

Section A. Independent Auditors

***Page 182*. Delete current note 4 and replace it with the following.**

In *NCP Litig. Tr. v. KPMG LLP*, the New Jersey Supreme Court observed that there often "can be difficulty in differentiating between whether the malfeasant conduct benefits or harms the corporation."[9] The court further observed that "inflating a corporation's revenues and enabling a corporation to continue in business "past the point of insolvency" cannot be considered a benefit to the corporation."[10] In *Cenco*, did the misconduct clearly benefit or harm the corporation?

***Page 182*. Renumber current question 6 as 7. Add new note 6.**

6. What effect will the *Cenco* decision likely have on the incentives of auditors?

[9] 901 A.2d 871, 887–88 (N.J. 2006).
[10] Id. at 888.

CHAPTER 6. EXECUTIVE COMPENSATION

Section A. Introduction and Overview

***Page 240*. Insert the following after the carryover paragraph**.

Restricted stock grants consist of an award of shares of the employer's common stock. The shares are restricted in that they subject to a vesting period. Until the shares vest, the recipient may not sell them. The vesting period can be determined either by the passage of time or the achievement of specified performance goals. Once the vesting period is completed, the recipient is free to hold or sell the shares. The grant is taxable income to the recipient, although the recipient can opt between paying ordinary income tax on the value of the shares when granted and then paying capital gains tax on the proceeds if and when the shares are eventually sold or paying ordinary income on the fair market value of the shares on the day they vest. The idea is that the grant will motivate the employee during the vesting period to increase the company's stock value. Unlike stock options, restricted stock does not have an expiration date, although most employees sell the shares promptly upon vesting.

In 2022, the SEC observed that:

> We estimate that about 45 percent of stock grants are subject to time-based vesting, though this has declined slightly (by about three percentage points) since [2015] with the growth in reliance on performance-contingent stock. Of the time-vesting stock awards, roughly one-third have cliff-vesting schedules while the vast majority of the remaining have graded vesting in annual increments.[472] For the stock awards that vest based on achieving performance conditions (approximately 55 percent of stock awards), the vast majority have cliff-vesting schedules. Approximately ten percent of awards with performance-based vesting also have an additional time-based vesting period at the end of the performance period. For option awards, the vast majority have time-based, graded vesting in annual increments.

***Page 242*. Insert the following after the carryover paragraph.**

In 2022, the SEC reported on the extent to which restricted stock grants and stock options were used by companies in the S&P 1500 index, which includes about 500 large cap corporations, 400 mid cap corporations, and 600 small cap corporations:

[472] About 95% of the awards with graded vesting vest in annual increments. [Ed.: Cliff vesting schedules give the employee ownership of all the shares subject to the grant on a single date at the end of the vesting period as opposed to vesting portions of the shares each year of the vesting period.]

	All Firms in Database	Firms in S&P 500	Firms in S&P MidCap 400	Firms in S&P SmallCap 600
Firms in Sample	1,694	497	393	580
Stock Grants to 2020 CEO:				
% of CEOs Granted Stock in 2020	81.0%	87.5%	85.0%	82.2%
Among subset of firms for which 2020 CEO was also CEO in 2019 and 2018:				
% of CEOs Granted Stock 0 out of Past 3 Years (2018-2020)	11.2%	8.7%	8.3%	11.7%
% of CEOs Granted Stock 1 out of Past 3 Years (2018-2020)	5.9%	4.6%	6.3%	5.5%
% of CEOs Granted Stock 2 out of Past 3 Years (2018-2020)	16.6%	14.2%	19.1%	16.3%
% of CEOs Granted Stock 3 out of Past 3 Years (2018-2020)	66.3%	72.5%	66.3%	66.5%
Stock Grants to Other 2020 NEOs:				
% of Firms that Granted Stock to Any NEO other than CEO in 2020	86.8%	92.6%	90.3%	88.4%
Among Firms that Made Such Grants, Average Number of Other NEOs Granted Stock in 2020	4.2	4.0	3.9	3.9

Table 1. Use of restricted stock grants by S&P 1500 firms

	All Firms in Database	Firms in S&P 500	Firms in S&P MidCap 400	Firms in S&P SmallCap 600
Firms in Sample	1,694	497	393	580
Option Grants to 2020 CEO				
% of CEOs Granted Options in 2020	22.4%	31.2%	20.9%	20.9%
Among subset of firms for which 2020 CEO was also CEO in 2019 and 2018:				
% of CEOs Granted Options 0 out of Past 3 Years (2018-2020)	61.5%	50.4%	59.8%	67.7%
% of CEOs Granted Options 1 out of Past 3 Years (2018-2020)	13.0%	12.3%	15.8%	12.4%
% of CEOs Granted Options 2 out of Past 3 Years (2018-2020)	14.7%	20.7%	14.5%	10.6%
% of CEOs Granted Options 3 out of Past 3 Years (2018-2020)	10.8%	16.6%	9.9%	9.3%
Option Grants to Other 2020 NEOs:				
% of Firms that Granted Options to Any NEO other than CEO in 2020	31.2%	42.1%	28.5%	29.1%
Among Firms that Made Such Grants, Average Number of Other NEOs Granted Options in 2020	3.1	3.3	3.1	2.8

Table 2. Use of stock options by S&P 1500 firms.

As the SEC observed, the analysis found "a significant drop, of greater than half, in the use of options to incentivize CEOs across all categories since" 2015, "which has largely been offset by an increase in the number and size of performance-contingent stock grants."[11]

***Page 243.* Insert the following after the carryover paragraph.**

Such concerns likely help explain the shift away from stock options and towards restricted stock grants.

[11] Pay Versus Performance, Exchange Act Release No. 95,607 128-29 (August 25, 2022).

Section D. Federal Law

***Page 317.* Delete all existing notes and questions and insert the following replacements**.

1. Dodd-Frank § 954 provided that:

> RECOVERY OF ERRONEOUSLY AWARDED COMPENSATION. The Securities Exchange Act of 1934 is amended by inserting after section 10C, as added by section 952, the following:
>
> > "SEC. 10D. RECOVERY OF ERRONEOUSLY AWARDED COMPENSATION POLICY.
> >
> > "(a) LISTING STANDARDS.—The Commission shall, by rule, direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that does not comply with the requirements of this section.
> >
> > "(b) RECOVERY OF FUNDS.—The rules of the Commission under subsection (a) shall require each issuer to develop and implement a policy providing—
> >
> > > "(1) for disclosure of the policy of the issuer on incentive-based compensation that is based on financial information required to be reported under the securities laws; and
> > >
> > > "(2) that, in the event that the issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer with any financial reporting requirement under the securities laws, the issuer will recover from any current or former executive officer of the issuer who received incentive-based compensation (including stock options awarded as compensation) during the 3-year period preceding the date on which the issuer is required to prepare an accounting restatement, based on the erroneous data, in excess of what would have been paid to the executive officer under the accounting restatement.".

In July 2015, the SEC issued a proposed rule implementing Dodd-Frank § 954, but it did not promulgate a final rule until October 2022.

In its adopting release, the SEC explained that:

> New Exchange Act Rule 10D-1 and the rule amendments adopted in this release supplement existing provisions by directing the exchanges to establish listing standards that require issuers to:
>
> - Develop and implement written policies for recovery of incentive-based compensation based on financial information required to be reported under the securities laws, applicable to the issuers' executive officers, during the three completed fiscal years immediately preceding the date that the issuer is required to prepare an accounting restatement; and
> - Disclose those compensation recovery policies in accordance with Commission rules, including providing the information in tagged data format.
>
> . . . Under the final rules, an issuer would be subject to delisting if it does not adopt and comply with its compensation recovery policy.[12]

---

[12] Listing Standards for Recovery of Erroneously Awarded Compensation, Exchange Act Rel. No. 96,159 (Oct. 26, 2022). [Ed.: Delisting means that the issuer's securities may no longer be traded on a stock exchange, significantly reducing the liquidity of the issuer's shares.]

Section 954 did not specify whether a clawback would be triggered by either so-called "Big R restatements," which correct errors that resulted in one or more material misstatements in prior financial statements, or a "Little r Restatement," which "correct errors that are not material to previously issued financial statements, but would result in a material misstatement if (a) the errors were left uncorrected in the current report or (b) the error correction was recognized in the current period . . .."[13] In the final rule, the SEC mandated that issuers adopt clawback policies triggered by either Big R or Little r restatements.

The executive officers who must be covered by the policy include "the issuer's president, principal financial officer, principal accounting officer (or if there is no such accounting officer, the controller), any vice-president of the issuer in charge of a principal business unit, division or function (such as sales administration or finance), any other officer who performs a policy-making function, or any other person who performs similar policy-making functions for the issuer."[14]

> In developing the definition of "executive officer" for purposes of Rule 10D-1, we considered the statutory purpose of the rule. First, Section 10D seeks to recover erroneously awarded incentive-based compensation, reducing a potential form of unjust enrichment, in which executive officers would gain from accounting errors at the expense of shareholders. The statute thus protects shareholders from bearing the economic burden of erroneously awarded compensation derived from material noncompliance with financial reporting requirements. The statute also helps to maintain investor confidence in markets and improve liquidity by incentivizing executive officers to provide more accurate financial reporting.[15]

Incentive-based compensation is defined as "any compensation that is granted, earned, or vested based wholly or in part upon the attainment of any financial reporting measure."[16] The amount of such compensation to be recovered under a compliant policy must be "'the amount of incentive-based compensation received by the executive officer or former executive officer that exceeds the amount of incentive-based compensation that otherwise would have been received had it been determined based on the accounting restatement,' computed without regard to taxes paid."[17]

> Applying this definition, after an accounting restatement, the issuer must first recalculate the applicable financial reporting measure and the amount of incentive-based compensation based thereon. The issuer must then determine whether, based on that financial reporting measure as calculated by relying on the original financial statements and taking into account any discretion that the compensation committee had applied to reduce the amount originally received, the executive officer received a greater amount of incentive-based compensation than would have been received applying the recalculated financial reporting measure. Where incentive-based compensation is based only in part on the achievement of a financial reporting measure performance goal, the issuer would first need to determine the portion of the original incentive-based compensation based on or derived from the financial reporting measure that was restated. The issuer would then need to recalculate the affected portion based on the financial reporting measure as restated, and

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[13] Id. at 28. The SEC further explained that:

> A "little r" restatement differs from a "Big R" restatement primarily in the reason for the error correction (as noted above), the form and timing of reporting, and the disclosure required. For example, a "Big R" restatement requires the issuer to file an Item 4.02 Form 8-K and to amend its filings promptly to restate the previously issued financial statements.81 In contrast, a "little r" restatement generally does not trigger an Item 4.02 Form 8-K, and an issuer may make any corrections "the next time the registrant files the prior year financial statements."

Id.

[14] Id. at 46.
[15] Id. at 49.
[16] Id. at 58.
[17] Id. at 75.

recover the difference between the greater amount based on the original financial statements and the lesser amount that would have been received based on the restatement.[18]

A compliant policy must require the issuer to pursue recovery of the specified amount. A board has no discretion to forego doing so absent a very limited exception for cases in which the direct costs of recovery would exceed the amount of the recovery. The issuer's board has limited discretion with respect to the timing of the recovery, provided it pursues the recovery reasonably promptly. The SEC noted that "an issuer may be acting reasonably promptly in establishing a deferred payment plan that allows the executive officer to repay owed erroneous compensation as soon as possible without unreasonable economic hardship to the executive officer, depending on the particular facts and circumstances," but declined to provide more detailed guidance.[19]

2. How does Dodd-Frank § 954 change the clawback rules under SOX § 304?

3. Former SEC Commissioner Troy Paredes argued that:

> Section 954 appears to operate as a "no-fault" provision—that is, Section 954 does not require that the restatement triggering the clawback be the result of any misconduct, which of course is to say that an individual may be required to forfeit some of his or her pay even if the executive committed no misdeed. By way of illustration, an executive who has worked diligently and honestly at a company that has robust financial controls and top-notch procedures and systems may nonetheless have to pay back a considerable portion of his or her compensation if the company has to restate because of an accounting error. I can understand why many might find this troubling.[20]

Does the SEC adoption of Rule 10D-1 confirm that § 954 and the issuer rules that must be adopted thereunder are "no fault" provisions?

4. What is the policy justification for recovering compensation from a CEO or CFO who was not personally involved in or at least aware of the misconduct that resulted in the restatement?

5. Is Rule 10D-1 too broad? Consider the following:

- The inclusion of Little r restatements.
- The inclusion of employees who a policy-making function for the issuer regardless of involvement with the events leading to the restatement.

6. Should the rule have given boards discretion not to pursue *de minimis* recoveries?

7. What might be the unintended consequences of SOX § 304? Put another way, how should rational corporate executives respond to these provisions when negotiating compensation with their employers?

8. Do the provisions of SOX § 304 and Dodd-Frank § 954 unduly intrude into the states' role as primary regulators of corporate governance? Are they consistent with the traditional dividing line between state corporate and federal securities law?

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[18] Id. at 75-76.

[19] Id. at 100.

[20] Troy Paredes, Remarks at Society of Corporate Secretaries & Governance Professionals, 66th National Conference on "The Shape of Things to Come" (July 13, 2012).

Page 310. **After the carryover paragraph insert the following.**

Pay Versus Performance, Exchange Act Release No. 95,607 (August 25, 2022)

I. INTRODUCTION

A. Background

Section 953(a) of the Dodd-Frank Act ("Section 953(a)") added Section 14(i) to the Exchange Act.[3] Section 14(i) mandates that the Commission shall, by rule, require each issuer to disclose in any proxy or consent solicitation material for an annual meeting of the shareholders of the issuer a clear description of any compensation required to be disclosed by the issuer under Item 402 of Regulation S-K (or any successor thereto), including, for any issuer other than an emerging growth company,* information that shows the relationship between executive compensation actually paid and the financial performance of the issuer, taking into account any change in the value of the shares of stock and dividends of the issuer and any distributions. Section 14(i) also states that an issuer may include a graphic representation of the information required to be disclosed.

In 2015, the Commission proposed a new rule to implement Section 953(a) by creating a new requirement in Item 402 of Regulation S-K. The proposed new item would require a registrant to provide a clear description of (1) the relationship between executive compensation actually paid to the registrant's named executive officers ("NEOs")* (including the registrant's principal executive officer (or persons acting in a similar capacity during the last completed fiscal year) ("PEO")) and the cumulative total shareholder return ("TSR") of the registrant, and (2) the relationship between the registrant's TSR and the TSR of a peer group chosen by the registrant, over each of the registrant's five most recently completed fiscal years.

. . .

We believe the disclosure mandated by Section 14(i) will allow investors to assess a registrant's executive compensation actually paid relative to its financial performance more readily and at a lower cost than under the existing executive compensation disclosure regime. Under Item 402 of Regulation S-K, which specifies the information that must be included when the applicable form or schedule requires executive compensation disclosure, specific information regarding financial performance is

[3] 15 U.S.C. 78a et seq. Subsequent to the addition of Section 14(i) to the Exchange Act, Section 102(a)(2) of the Jumpstart Our Business Startups Act amended Section 14(i) to exclude registrants that are "emerging growth companies" from the pay-versus-performance disclosure requirements. Pub. L. 112-106, 126 Stat. 306 (2012).

* [Ed.: In a subsequent footnote, the SEC explained that:

> "Emerging growth company" means an issuer that had total annual gross revenues of less than $1.07 billion during its most recently completed fiscal year. An issuer that is an emerging growth company as of the first day of that fiscal year shall continue to be deemed an emerging growth company until the earliest of: (i) the last day of the fiscal year of the issuer during which it had total annual gross revenues of $1.07 billion or more; (ii) the last day of the fiscal year of the issuer following the fifth anniversary of the date of the first sale of common equity securities of the issuer pursuant to an effective registration statement under the Securities Act of 1933; (iii) the date on which such issuer has, during the previous three year period, issued more than $1 billion in non-convertible debt; or (iv) the date on which such issuer is deemed to be a large accelerated filer. Section 102(a)(2) of the Jumpstart Our Business Startups Act amended Section 14(i) to exclude registrants that are EGCs from the pay-versus-performance disclosure requirements. In accordance with this provision, the Commission did not propose to require EGCs to provide pay-versus-performance disclosure.]

* [Ed.: In a subsequent footnote, the SEC explained that:

> 17 CFR 229.402(a)(3) defines the NEOs for whom Item 402 of Regulation S-K executive compensation is required as (1) all individuals serving as the registrant's PEO during the last completed fiscal year, regardless of compensation level, (2) all individuals serving as the registrant's principal financial officer or acting in a similar capacity during the last completed fiscal year ("PFO"), regardless of compensation level, (3) the registrant's three most highly compensated executive officers other than the PEO and PFO who were serving as executive officers at the end of the last completed fiscal year, and (4) up to two additional individuals for whom Item 402 of Regulation S-K disclosure would have been provided but for the fact that the individual was not serving as an executive officer of the registrant at the end of the last completed fiscal year. Because the pay-versus-performance disclosure was proposed as new paragraph (v) to Item 402 of Regulation S-K, the disclosure also would be required for the NEOs.]

already required, including in the Performance Graph in 17 CFR 229.201(e) ("Item 201(e) of Regulation S-K"), the Supplementary Financial Information in 17 CFR 229.302 (Item 302), and Management's Discussion and Analysis of Financial Condition and Results of Operations in 17 CFR 220.303 (Item 303). In addition, Item 402 of Regulation S-K also requires detailed disclosure of executive compensation and principles-based disclosure requirements regarding the relationship between pay and performance.[14]

There is no single place, however, where issuers must provide investors with direct comparisons of an executive's pay with their company's performance, and specifically financial performance, particularly if investors are interested in that comparison over a timespan longer than the most recent reporting period. . . .

Section 14(i) did not expressly prescribe the manner in which issuers would disclose the required information and we have exercised our discretion to provide for a consistent format that we believe furthers the statutory objectives of making pay-versus-performance data clear and easy for investors to evaluate. Standardizing the format and presentation of data, in particular quantitative metrics, to promote such ease of use requires incremental costs for issuers. We have elected not to pursue a wholly principles-based approach because, among other reasons, such a route would limit comparability across issuers and within issuers' filings over time, as well as increasing the possibility that some issuers would choose to report only the most favorable information. . . .

B. Overview of Final Amendments

The amendments add new 17 CFR 229.402(v) ("Item 402(v) of Regulation S-K"), which requires registrants to describe the relationship between the executive compensation actually paid by the registrant and the financial performance of the registrant over the time horizon of the disclosure. Item 402(v) of Regulation S-K requires disclosure of the cumulative TSR of the registrant . . ., the TSR of the registrant's peer group, the registrant's net income, and a measure chosen by the registrant and specific to the registrant ("Company-Selected Measure") as the measures of financial performance.

The final rules require the following tabular disclosures, with the asterisked items indicating portions of the final rules from which smaller reporting companies ("SRCs")[19] are exempt:

[14] The Compensation Discussion and Analysis ("CD&A") required by 17 CFR 229.402(b) ("Item 402(b) of Regulation S-K") requires registrants to provide an explanation of "all material elements of the registrant's compensation of the named executive officers." 17 CFR 229.402(b)(1). With respect to performance, Item 402(b)(2) of Regulation S-K includes non-exclusive examples of information that may be material, including (i) specific items of corporate performance taken into account in setting compensation policies and making compensation decisions; (ii) how specific forms of compensation are structured and implemented to reflect these items of the registrant's performance; and (iii) how specific forms of compensation are structured and implemented to reflect the NEO's individual performance and/or individual contribution to these items of the registrant's performance.

[19] A "smaller reporting company" means, in the case of issuers required to file reports under Sections 13(a) or 15(d) of the Exchange Act, an issuer that is not an investment company, an asset-backed issuer, or a majority-owned subsidiary of a parent that is not a smaller reporting company and that: (1) had a public float of less than $250 million (as of the last business day of the issuer's most recently completed second fiscal quarter); or (2) had annual revenues of less than $100 million (as of the most recently completed fiscal year for which audited financial statements are available) and either: (i) no public float (as of the last business day of the issuer's most recently completed second fiscal quarter); or (ii) a public float of less than $700 million (as of the last business day of the issuer's most recently completed second fiscal quarter). 17 CFR 240.12b-2; and 17 CFR 229.10. Business development companies ("BDCs"), which are a type of closed-end investment company that is not registered under the Investment Company Act, do not fall within the SRC definition, and thus do not qualify for the scaled disclosures that we are adopting for SRCs. See infra Section II.G (discussing our considerations with respect to SRC disclosure requirements).

Year	Summary Compensation Table Total for PEO	Compensation Actually Paid to PEO	Average Summary Compensation Table Total for Non-PEO NEOs	Average Compensation Actually Paid to Non-PEO NEOs	Value of Initial Fixed $100 Investment Based On:		Net Income	[Company-Selected Measure]*
					Total Shareholder Return	Peer Group Total Shareholder Return*		
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)
Y1								
Y2								
Y3								
Y4*								
Y5*								

In addition, registrants are required to use the information in the above table to provide clear descriptions of the relationships between compensation actually paid and three measures of financial performance, as follows: describe the relationship between (a) the executive compensation actually paid to the registrant's PEO and (b) the average of the executive compensation actually paid to the registrant's remaining NEOs to (i) the cumulative TSR of the registrant, (ii) the net income of the registrant, and (iii) the registrant's Company-Selected Measure, in each case over the registrant's five most recently completed fiscal years. Registrants are also required to provide a clear description of the relationship between the registrant's TSR and the TSR of a peer group chosen by the registrant, also over the registrant's five most recently completed fiscal years. Registrants have flexibility as to the format in which to present the descriptions of these relationships, whether graphical, narrative, or a combination of the two. Registrants will also have the flexibility to decide whether to group any of these relationship disclosures together when presenting their clear description disclosure, but any combined description of multiple relationships must be "clear." SRCs will only be required to present such clear descriptions with respect to the measures they are required to include in the table and for their three, rather than five, most recently completed fiscal years.

A registrant that is not an SRC also will be required to provide an unranked list of the most important financial performance measures used by the registrant to link executive compensation actually paid to the registrant's NEOs during the last fiscal year to company performance. Although, as discussed below, registrants may include non-financial performance measures in this list, they must select the Company-Selected Measure from the financial performance measures included in this list, and it must be the financial performance measure that in the registrant's assessment represents the most important performance measure (that is not otherwise required to be disclosed in the table) used by the registrant to link compensation actually paid to the registrant's NEOs, for the most recently completed fiscal year, to company performance.

. . .

II. DISCUSSION OF FINAL AMENDMENTS

A. New Item 402(v) of Regulation S-K

. . . [W]e are adopting the requirement to include the new Item 402(v) of Regulation S-K disclosure in any proxy or information statement for which disclosure under Item 402 of Regulation S-K is

required. . . . We are not requiring the pay-versus-performance disclosure in other filings where disclosure under Item 402 of Regulation S-K is required, as we believe that, taken in context, the language of Section 14(i) calling for registrants to provide the disclosure "in any proxy or consent solicitation material for an annual meeting of the shareholders" suggests that the information was intended to be presented in conjunction with a shareholder vote.

. . .

The final rules provide registrants flexibility in determining where in the proxy or information statement to provide the disclosure required, as proposed. We believe . . . that mandating registrants to include the disclosure in the CD&A may cause confusion by suggesting that the registrant considered the pay-versus-performance relationship in its compensation decisions, which may or may not be the case.

. . . The simplicity of the tabular disclosure should allow investors to more easily understand and analyze the relationship between pay and performance. In addition, registrants can supplement the tabular disclosure, so long as any additional disclosure is clearly identified as supplemental, not misleading, and not presented with greater prominence than the required disclosure. We also believe the simplicity of the tabular disclosure matches the requirement in Section 14(i) that registrants provide a ""clear description" of their pay-versus-performance, and, consistent with Section 14(i), will better allow investors to compare disclosures within companies over time and across companies, making the disclosure more useful.

. . . [R]egistrants must also provide a narrative, graphical, or combined narrative and graphical description of the relationships between executive compensation actually paid and the registrant's TSR, and between the registrant's TSR and peer group TSR. We believe the disclosure of the relationship between executive compensation actually paid and TSR will satisfy the language of Section 14(i) that registrants disclose the "relationship" between executive compensation and registrant performance. Further, . . . we believe disclosure about the relationship between registrant TSR and peer group TSR may provide a useful point of comparison to assess the relationship between the registrant's executive compensation actually paid and its financial performance compared to the performance of its peers during the same time period.[69]

C. Determination of Executive Compensation Actually Paid

. . .

We believe that it is appropriate to include pension compensation in the calculation of compensation "actually paid." The adopted approach in particular provides an appropriate measure for purposes of determining compensation "actually paid" during the applicable year because it reflects the benefits an executive may expect to receive based on additional service the executive provided during the year (or service cost), and it incorporates additional benefits attributable to changes in the pension contract between the executive and the company (or prior service cost). In many cases, this measure will approximate the value that would be set aside currently by the registrant to fund the pension benefits payable upon retirement for the service provided, and any plan amendments made, during the applicable year. In addition, the inclusion of pension compensation is consistent with other compensation disclosure requirements, such as Item 402(c) of Regulation S-K. These same rationales apply whether or not the pension amounts are vested. Consistent with the equity compensation adjustment, the pension adjustment will be included even when unvested until an officer leaves the company.

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[69] Peer comparisons are a component companies often use to assess the performance of their executives. See, e.g., John Bizjak, Swaminathan Kalpathy, Zhichuan Frank Li, & Brian Young, The Choice of Peers for Relative Performance Evaluation in Executive Compensation, 26 REV. FIN. __ (forthcoming 2022), available athttps://papers.ssrn.com/sol3/papers.cfm?abstract_id=2833309 (finding that, in a sample of the largest 750 U.S. companies (by market capitalization), "over 50%" of companies in 2017 used performance awards based on performance relative to a peer group, "comprising approximately one-third of the value of total compensation").

D. Measures of Performance

. . .

We are adopting the requirement . . . that all registrants subject to the final rules use TSR, and that registrants (other than SRCs) use peer group TSR, as measures of performance. As noted in the Proposing Release, . . . we believe that TSR is consistent with that statutory language. In addition, we believe mandating a consistently calculated measure for all registrants will further the comparability of the pay-versus-performance disclosures across registrants, as noted by some commenters.

. . .

We also believe that absolute company performance alone, as reflected in TSR, may not be a sufficient basis for comparison between companies, and that peer group TSR will provide investors with more comprehensive information for assessing whether the registrant's performance was driven by factors common to its peers or instead by the registrant's own strategy and other choices. The final rules require a registrant to disclose weighted peer group TSR (weighted according to the respective issuers' stock market capitalization at the beginning of each period for which a return is indicated), using either the same peer group used for purposes of Item 201(e) of Regulation S-K or a peer group used in the CD&A for purposes of disclosing registrants' compensation benchmarking practices. If the peer group is not a published industry or line-of-business index, the identity of the issuers composing the group must be disclosed in a footnote. A registrant that has previously disclosed the composition of issuers in its peer group in prior filings with the Commission would be permitted to comply with this requirement by incorporation by reference to those filings. We believe this would avoid the potential for duplicative disclosure.

. . . [T]o address commenters' concerns with respect to the proposal to use TSR and peer group TSR as the sole measures of performance (such as causing companies to adjust their compensation programs to more heavily rely on TSR), we are also requiring registrants to include net income and a Company-Selected Measure as performance measures in the tabular disclosure, and also permitting companies to voluntarily include additional measures of their choosing in the table, as suggested by some commenters. The inclusion of the Company-Selected Measure and the ability of registrants to voluntarily include additional measures may also address commenters' concerns with respect to incentivizing short-term performance at the expense of shareholders' long-term best interests. We believe these additional measures should help alleviate concerns expressed by some commenters that disclosing only TSR (for a registrant and its peer group) would put too much emphasis on that one measure.

NOTES AND QUESTIONS

1. Dodd-Frank § 953(a) mandated a "clear description" of executive compensation's relationship to performance. Do the disclosures required by the Release satisfy that mandate?

2. The SEC explained that it had opted against "a wholly principles-based approach" in favor of a mainly rules-based approach.

> A common analytical approach to classifying laws as rules or principles uses their temporal orientation. It distinguishes when content is provided: rules define boundaries ex ante, while principles define them ex post. . . . Thus, rules and principles are sometimes classified according to how much guidance they provide to actors ex ante--how much certainty is provided. Notably, under this view, both rules and principles can be either complex or simple.
>
> . . .
>
> A more conceptual classification views rules and principles in terms of designated attributes such as their relative generality versus specificity, abstractness versus concreteness, and universality versus particularity. Provisions characterized by generality,

abstractness, or universality are principles, while those that are specific, concrete, and particular are rules.

. . .

Finally, a functional approach to classifying a legal or accounting provision as a rule or a principle considers the scope of discretion reposed in designated actors. The more discretion a provision reposes, the more it is principle-like, and the less discretion reposed, the more it is rule-like.

Did § 953 contemplate a rules-based or a principles-based approach? Does the difference matter?

3. In the Release, the SEC acknowledged that:

> The registrants that will be subject to the final rules must currently comply with Item 402 of Regulation S-K, which requires the disclosure of extensive information about the compensation of NEOs, and, except in the case of SRCs, with Item 201(e) of Regulation S-K, which requires graphical disclosure of registrant TSR and peer group TSR. They are also subject to financial statement and disclosure requirements under Regulation S-X. The underlying information necessary to provide the required pay-versus-performance disclosure is, with limited exceptions discussed below, already encompassed by these existing disclosure requirements. However, the existing disclosures might not present the underlying information in a format that allows investors to readily assess the alignment of pay and performance.
>
> Under the final rules, the definition of executive compensation actually paid for a fiscal year is, generally,424 total compensation as reported in the Summary Compensation Table for that year (i) less the change in the actuarial present value of pension benefits,425 (ii) less the grant-date fair value of any stock and option awards granted during that year, (iii) plus the pension service cost for the year and, in the case of any plan amendments (or initiations), the associated prior service cost (or less any associated credit), and (iv) plus the change in fair value of outstanding and unvested stock and option awards during that year (or as of the vesting date or the date the registrant determines the award will not vest, if within the year) as well as the fair value of new stock and option awards granted during that year as of the end of the year (or as of the vesting date or the date the registrant determines the award will not vest, if within the year). Adjustments (i) and (iii) with respect to pension plans will not apply to SRCs because they are not otherwise required to disclose executive compensation related to pension plans.

Does the amendment to Item 402 change the information available to investors or simply the way it is presented?

4. What are the advantages and disadvantages of using TSR as a required financial performance measure?

5. Will the disclosures accurately inform shareholders of the executive compensation that was actually paid?

6. The new disclosures will further lengthen the executive compensation section of annal proxy statements. Is that additional length a cost for investors? How will it impact investor incentives?

7. Why did Congress exempt EGCs from the § 953(a) rules? Why did the SEC allow SRCs to make less extensive disclosures?

8. What will likely be the greatest challenge for companies complying with the new disclosures?

9. Will companies need to subject the processes used to prepare these disclosures to the SOX § 404 managerial assessment and, if applicable, the auditor attestation? What about the §§ 302 and 906 certification requirements?

CHAPTER 8. INSIDER TRADING

Section C. Compliance Programs

***Page 421.* Insert the following after the first paragraph:**

In 2022, the SEC responded to such concerns by amending Rule 10b5-1 in several respects. As amended, the safe harbor is available only for plans that include a cooling-off period between adoption of the plan and the first trade executed pursuant to it. In the case of officers and directors of the issuer, the cooling-off period is the later of either ninety days after the plan's adoption or two business days after the issuer files a Form 10-Q or Form 10-K. For other insiders of the issuer, the cooling-off period is 30 days after its adoption. Directors or officers of the issuer must include in the plan a written representation that they were unaware of material nonpublic information (presumably as of the time the plan is adopted) and adopted the plan in good faith. Persons subject to the Rule may only have one plan in place at a time, thereby closing the former loophole allowing persons other than the issuer to use multiple overlapping Rule 10b5-1 plans. To prevent insiders from using sequential single-trade plans, which allegedly allowed insiders to game the timing of plan adoptions and transactions, the amended rule permits subject persons to use only one single-trade plan during any consecutive 12-month period. Finally, as amended, the Rule requires that all persons entering into a Rule 10b5-1 plan must act in good faith with respect to that plan when trading.[21] The prior version of the rule had only explicitly required that the insider act in good faith when adopting the plan. As amended, the rule imposes a continuous duty of good faith through the life of the plan, thereby including trades executed in pursuance to the plan.

The 2022 amendments to Rule 10b5-1 also require new corporate disclosures with respect to trading plans adopted by directors and officers of the issuer. Companies must annually disclose whether they have insider trading policies and procedures governing trading by their directors, officers and employees. If so, those policies must be included as an exhibit to the company's annual report on Form 10-K as filed with the SEC.

In addition, an issuer will have to disclose in its Form 10-Q quarterly reports and its Form 10-K annual report whether any officer or director adopted, amended, or terminated a Rule 10b5-1 trading plan during the preceding quarter. The company must also disclose the material terms of each such plan, including the identity of the adopter, the date the plan was adopted, modified, or terminated, and the amount (but not the price) of securities traded pursuant to the plan.

[21] Insider Trading Arrangements and Related Disclosures, Exchange Act Release No. 96,492 (Dec. 14, 2022).

CHAPTER 9. VOTING AND PROXIES

B. Federal Proxy Regulation

***Page 488*. Add at the top of the page above the SEC Release title**.

Universal Proxy, Exchange Act Release No. 93,596 (Nov. 17, 2021)

. . . Shareholders voting in person at a meeting may select among all of the duly nominated director candidates proposed for election by any party in an election contest and vote for any combination of those candidates. Shareholders voting by proxy, however, do not have this same flexibility. The interplay between state and Federal law means that shareholders voting by proxy generally are unable to choose a mix of dissident and registrant nominees. The dissident and registrant each send a proxy card to shareholders, with the registrant's proxy card typically listing only the registrant's nominees and the dissident's proxy card typically listing only the dissident's nominees. . . .

[Our] final rules:

- Require the use of a universal proxy card by all participants in a non-exempt director election contest. The universal proxy card must include the names of both registrant and dissident nominees, along with certain other shareholder nominees included as a result of proxy access;
- Expand the determination of a "bona fide nominee" to include a person who consents to being named in any proxy statement for a registrant's next shareholder meeting for the election of directors;
- Require dissidents to provide registrants with notice of their intent to solicit proxies and to provide the names of their nominees no later than 60 calendar days before the anniversary of the previous year's annual meeting;
- Require registrants to notify dissidents of the names of the registrants' nominees no later than 50 calendar days before the anniversary of the previous year's annual meeting;*
- Require dissidents to file their definitive proxy statement by the later of 25 calendar days before the shareholder meeting or five calendar days after the registrant files its definitive proxy statement;
- Require each side in a proxy contest to refer shareholders to the other party's proxy statement for information about the other party's nominees and refer shareholders to the Commission's website to access the other side's proxy statement free of charge;
- Require that dissidents solicit the holders of shares representing at least 67% of the voting power of the shares entitled to vote at the meeting; and
- Establish presentation and formatting requirements for universal proxy cards that ensure that each party's nominees are presented in a clear, neutral manner.

We also are adopting . . . changes to the form of proxy and proxy statement disclosure requirements applicable to all director elections. These amendments:

- Require proxy cards to include an "against" voting option in director elections, when there is a legal effect to a vote against a director nominee;
- Require that the proxy card provide shareholders with the ability to "abstain" in a director election where a majority voting standard applies; and
- Require proxy statement disclosure about the effect of a "withhold" vote in an election of directors.

. . .

* [Ed.: The new SEC rules do not preempt state laws allowing corporations' articles or bylaws to include advance notice requirements or nomination procedures.]

In response to commenters arguing for an optional universal proxy system, an optional system without additional accompanying rule changes would raise problems not presented by a mandatory requirement, such as issues related to how and when shareholders presented with a universal proxy card would access information about the other party's nominees in order to make an informed voting decision. Mandating a universal proxy in all non-exempt election contests is less likely to cause shareholder confusion than an optional system which would operate differently, depending on whether one or both sides elected to opt in or opt out of universal proxy. . . .

. . . We view the arguments that mandatory universal proxy will lead to distraction for registrants, hamstring directors, and lead to greater ""balkanization" of boards of directors as unpersuasive. Even with the use of universal proxy cards, registrants and dissidents will retain the same ability to advocate the election of their nominees and raise concerns about negative boardroom dynamics that they have today. Shareholders will continue to have the ability to evaluate these concerns, including potential "balkanization" of the board, when they make their voting decisions. The rule amendments we are adopting are intended to improve the mechanics of the proxy voting process, not influence its outcome. Further, it is not apparent that allowing shareholders to more easily base their vote on individual and collective characteristics of board candidates, rather than forcing an "either or" choice between dissident or registrant nominees, would negatively impact registrants or boardroom dynamics. . . . Lastly, even if the use of universal proxy will lead to greater frequency of "split" boards, it is unclear whether that effect will necessarily lead to detrimental changes in board dynamics, with some viewing a diversity of viewpoints among board members as a positive development. The mandatory use of universal proxy cards will permit shareholders to choose their preferred mix of directors, taking into consideration both complementary skill sets and other board dynamics.

For the same reason, we do not believe the universal proxy requirement we are adopting will result in promoting the interests of special interest groups and short term activists, at the expense of shareholders generally. Even with the use of universal proxy cards, a dissident must ultimately persuade shareholders that its agenda is in their best interests in order to successfully elect its nominees. Moreover, if elected to the board of directors, such dissident nominees will be subject to the same state-law fiduciary duties to the corporation and, and by extension, all of its shareholders as all other directors, many of whom are also commonly affiliated with other entities.

. . .

The additional disclosure and presentation provisions adopted in this document and described in greater detail below will help to avoid some of the concerns of those who do not favor mandatory universal proxies. For example, participants in a contested election will not be required to include information about the opposing side's nominees in their own proxy statement. Rather, each side's proxy statement must direct shareholders to the opposing side's proxy statement for information about that participant's nominees. Each universal proxy card will be subject to the formatting and presentation requirements in the revised rules we adopt in this document. These requirements are intended to ensure that each side's nominees are grouped together and clearly identified as such, and presented in a fair and impartial manner. In addition, each universal proxy card must disclose the treatment of proxy cards containing over-votes and under-votes. These disclosure and presentation mandates in our rule amendments are intended to avoid shareholder confusion that could result in an increase in defective ballots and shareholder disenfranchisement. As shareholders become more familiar with universal proxy cards in director election contests, any initial confusion will likely abate. While we are mindful of the arguments that mandated universal proxy could have unintended consequences with respect to the mechanics of voting, the safeguards described above are intended to reduce that possibility.

. . . [A] universal proxy requirement without a minimum solicitation requirement could enable dissidents to capitalize on the registrant's solicitation efforts while relieving dissidents of the time and expense necessary to undertake meaningful solicitation efforts, thereby potentially exposing registrants to frivolous proxy contests. The minimum solicitation requirement establishes a fundamentally important check in that regard.

After careful consideration of the many comments received on this topic, and an updated economic analysis of the costs and benefits of setting the minimum solicitation threshold at various levels, we have decided to adopt the requirement that dissidents solicit holders of shares representing at least 67% of the voting power of shares entitled to vote on the election of directors. We have raised the threshold from a majority of the voting power to 67% of the voting power in response to commenters' concerns that setting the threshold at the proposed majority of the voting power would insufficiently deter the potential for "freeriding" of dissident nominees on the registrant's proxy card. A 67% threshold represents an appropriate balance between achieving the benefits of the universal proxy requirement for shareholders and preventing dissidents from capitalizing on the inclusion of dissident nominees on the registrant's universal proxy card without undertaking meaningful solicitation efforts. Comments from a wide range of market participants . . . indicated that a 67% threshold enjoys broad support and represents a reasonable compromise between the competing policy objectives related to this topic.

The increase in the dissident minimum solicitation requirement to 67% should mitigate concerns that the originally-proposed threshold would have incentivized dissidents to solicit only the minimum number of shareholders while ignoring all others, particularly retail shareholders with small holdings. Notably, our analysis of data provided by a proxy services provider demonstrates that dissidents overwhelmingly tend to solicit a substantial majority of voting power despite not being subject to any minimum solicitation threshold in contested elections. We agree that a higher threshold better incentivizes dissidents to engage and solicit votes from more shareholders without imposing an undue burden on dissidents. As a practical matter, those shareholders who are not solicited by the dissident will receive the registrant's proxy materials with the names of the dissident's nominees and information on how to access the dissident's materials on the Commission's website. Therefore, those shareholders who wish to do so can take steps to access information about dissident nominees before exercising their vote, whether or not they are solicited by the dissident. As noted above, current proxy rules do not require a dissident to solicit any minimum number of shareholders, so the 67% minimum solicitation threshold we are adopting represents an important step forward in establishing a minimum requirement for dissidents to engage with shareholders.

NOTES AND QUESTIONS

1. As discussed in more detail in Chapter 11, proxy contests can involve a full slate, in which the dissident seeks to replace the entire incumbent board with new directors, or a short slate, in which the dissident seeks only to replace a minority of the incumbent board. A dissident who wants control of the corporation will conduct a full slate contest, while a dissident who simply seeks a seat at the table—i.e., influence—will conduct a short slate. Will the availability of a universal proxy increase the frequency of full and/or short slate contests?

2. Is the SEC correct that the universal proxy will not confuse shareholders? Consider the sample universal proxy cards reprinted below.

Note on Universal Proxy Card Forms

As adopted by the Universal Proxy release, Rule 14a-19(e) imposes additional proxy card formatting requirements applicable to universal proxy cards. As summarized in the release, these requirements include:

- The proxy card must set forth the names of all duly nominated director candidates;
- The proxy card must provide a means for shareholders to grant authority to vote for the nominees set forth;
- The proxy card must clearly distinguish among registrant nominees, dissident nominees, and any proxy access nominees;
- Within each group of nominees, the nominees must be listed in alphabetical order by last name on the proxy card;
- The same font type, style and size must be used to present all nominees on the proxy card;

- The proxy card must prominently disclose the maximum number of nominees for which authority to vote can be granted; and
- The proxy card must prominently disclose the treatment and effect of a proxy executed in a manner that grants authority to vote for more nominees than the number of directors being elected, in a manner that grants authority to vote for fewer nominees than the number of directors being elected, or in a manner that does not grant authority to vote with respect to any nominees.

A proxy contest launched by hedge fund Land & Buildings Investment Management, LLC (L&B), at Apartment Investment & Management Co. (AIMC) provided an early example of how the new requirements will work. AIMC's card was printed on white stock, while L&B's was printed on blue stock.

Note that both cards include voting recommendations. Note also that both sides cards recommend using that side's card even if the shareholder plans to vote for the other side's nominees. Presumably, both sides want to know if a shareholder has voted for the other side so that they can contact the shareholder to try to change their mind.

Apartment Investment and Management Company **WHITE PROXY CARD**

THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" ALL THREE (3) COMPANY NOMINEES AND NOT TO VOTE FOR ANY OF THE REMAINING TWO (2) LAND & BUILDINGS NOMINEES LISTED IN PROPOSAL 1 BELOW.

1. To elect three (3) directors, for a term of two years each, to serve until the 2024 Annual Meeting of Stockholders and until their successors are duly elected and qualified – Vote "FOR" up to three (3) nominees in total. You are permitted to vote for fewer than three (3) nominees. If you vote "FOR" fewer than three (3) nominees, your shares will only be voted "FOR" those nominees you have so marked. If you vote "FOR" more than three (3) nominees, all of your votes on Item 1 will be invalid and will not be counted.

COMPANY NOMINEES

The Board of Directors recommends a vote "FOR" the following three (3) Company Nominees:

	FOR	WITHHOLD
(1A) Jay Paul Leupp	❑	❑
(1B) Michael A. Stein	❑	❑
(1C) R. Dary Stone	❑	❑

LAND & BUILDINGS NOMINEES OPPOSED BY THE COMPANY

The Board of Directors recommends that you do NOT vote for any of the following two (2) Land & Buildings Nominees:

	FOR	WITHHOLD
(1D) Michelle Applebaum	❑	❑
(1E) James P. Sullivan	❑	❑

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR PROPOSALS 2 AND 3.

2. To ratify the selection of Ernst & Young LLP to serve as the independent registered public accounting firm for the Company for the fiscal year ending December 31, 2022.

❑ **FOR** ❑ **AGAINST** ❑ **ABSTAIN**

3. To conduct an advisory vote on executive compensation.

❑ **FOR** ❑ **AGAINST** ❑ **ABSTAIN**

Continued and to be signed on the reverse side

Figure 4. AIMC Universal Proxy Statement (front).

APARTMENT INVESTMENT AND MANAGEMENT COMPANY **WHITE PROXY CARD**

ANNUAL MEETING OF STOCKHOLDERS

THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS FOR THE ANNUAL MEETING OF STOCKHOLDERS – December 16, 2022 AT 9:00 A.M. MOUNTAIN TIME

The undersigned hereby appoints Wes Powell, H. Lynn C. Stanfield, and Jennifer Johnson and each of them the undersigned's true and lawful attorneys and proxies (with full power of substitution in each) to vote all Common Stock of Apartment Investment and Management Company ("Aimco"), standing in the undersigned's name, at the Annual Meeting of Stockholders of Aimco to be held on Friday, December 16, 2022 at 9:00 a.m., Mountain Time, at Aimco's corporate headquarters, 4582 South Ulster Street, Suite 1450, Denver, CO 80237, and any adjournment or postponement thereof (the "Stockholders' Meeting"), upon those matters as described in the Proxy Statement for the Stockholders' Meeting.

This Proxy Card when properly executed will be voted in the manner directed herein. If you mark a vote with respect to less than three (3) nominees in Proposal 1, your shares will only be voted FOR those nominees you have so marked. If you vote FOR more than three (3) nominees, all of your votes on Proposal 1 will be invalid and will not be counted. If this proxy is executed but voting instructions are not marked with respect to a proposal, this proxy will be voted "FOR" each of the Company nominees in Proposal 1, and "FOR" Proposals 2 and 3. In their discretion, the proxies are authorized to vote upon such other business as may properly come before the Stockholders' Meeting (including and adjournment or postponement thereof).

Signature

Date

Title or Authority

Signature if Held Jointly

NOTE: Please sign exactly as name(s) appear(s) hereon. When signing as attorney, executor, administrator or other fiduciary, please give full title as such. Joint owners should each sign personally. All holders must sign. If a corporation or partnership, please sign in full corporate or partnership name by authorized officer.

(Continued and to be marked on the other side)

Figure 5. AIMC Universal Proxy Card (reverse)

PRELIMINARY COPY SUBJECT TO COMPLETION
DATED OCTOBER 14, 2022

APARTMENT INVESTMENT AND MANAGEMENT COMPANY

2022 ANNUAL MEETING OF STOCKHOLDERS

THIS PROXY IS SOLICITED ON BEHALF OF LAND & BUILDINGS CAPITAL GROWTH FUND, LP, AND THE OTHER PARTICIPANTS IN ITS PROXY SOLICITATION

THE BOARD OF DIRECTORS OF APARTMENT INVESTMENT AND MANAGEMENT COMPANY IS NOT SOLICITING THIS PROXY

P R O X Y

The undersigned appoints Jonathan Litt, Craig Melcher and John Ferguson, and each of them, as attorneys and agents with full power of substitution to vote all shares of Class A Common Stock (the "Common Stock"), of Apartment Investment and Management Company (the "Company" or "Aimco") which the undersigned would be entitled to vote if personally present at the 2022 annual meeting of stockholders of the Company scheduled to be held at 9:00 a.m., Mountain Time, on December 16, 2022, at 4582 South Ulster Street, Suite 1450, Denver, Colorado 80237 (including any adjournments or postponements thereof and any meeting called in lieu thereof, the "Annual Meeting").

The undersigned hereby revokes any other proxy or proxies heretofore given to vote or act with respect to the shares of Common Stock of the Company held by the undersigned, and hereby ratifies and confirms all action the herein named attorneys and proxies, their substitutes, or any of them may lawfully take by virtue hereof. If properly executed, this Proxy will be voted as directed on the reverse and in the discretion of the herein named attorneys and proxies or their substitutes with respect to any other matters as may properly come before the Annual Meeting that are unknown to Land & Buildings Capital Growth Fund, LP ("Land & Buildings") a reasonable time before this solicitation.

THIS PROXY WILL BE VOTED AS DIRECTED. IF NO DIRECTION IS INDICATED WITH RESPECT TO THE PROPOSALS ON THE REVERSE, THIS PROXY WILL BE VOTED "FOR" THE TWO (2) LAND & BUILDINGS NOMINEES AND "FOR" ONE (1) COMPANY NOMINEE UNOPPOSED BY LAND & BUILDINGS IN PROPOSAL 1, "FOR" PROPOSAL 2 AND "AGAINST" PROPOSAL 3.

This Proxy will be valid until the completion of the Annual Meeting. This Proxy will only be valid in connection with Land & Buildings solicitation of proxies for the Annual Meeting.

Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting:
This Proxy Statement and our BLUE universal proxy card are available at http:/www.___________.com.

IMPORTANT: PLEASE SIGN, DATE, AND MAIL THIS PROXY CARD PROMPTLY!

CONTINUED AND TO BE SIGNED ON REVERSE SIDE

Figure 6. L&B Universal Proxy Card (front)

[X] Please mark vote as in this example

LAND & BUILDINGS STRONGLY RECOMMENDS THAT STOCKHOLDERS VOTE "FOR" THE TWO LAND & BUILDINGS NOMINEES AND "FOR" ONE COMPANY NOMINEE UNOPPOSED BY LAND & BUILDINGS, AND NOT TO VOTE "FOR" EITHER OF THE REMAINING TWO COMPANY NOMINEES LISTED BELOW IN PROPOSAL 1.

YOU MAY SUBMIT VOTES "FOR" UP TO THREE NOMINEES IN TOTAL. YOU ARE PERMITTED TO VOTE FOR LESS THAN THREE NOMINEES. IMPORTANTLY, IF YOU MARK MORE THAN THREE "FOR" BOXES WITH RESPECT TO THE ELECTION OF DIRECTORS, ALL OF YOUR VOTES FOR THE ELECTION OF DIRECTORS WILL BE DEEMED INVALID. IF YOU MARK FEWER THAN THREE "FOR" BOXES WITH RESPECT TO THE ELECTION OF DIRECTORS, THIS PROXY CARD, WHEN DULY EXECUTED, WILL BE VOTED ONLY "FOR" THOSE NOMINEES YOU HAVE SO MARKED.

1. Election of three nominees to serve as directors until the Company's 2024 annual meeting of stockholders and until their successors have been duly elected and qualified.

LAND & BUILDINGS NOMINEES	**FOR**	**WITHHOLD**
a) Michelle Applebaum	☐	☐
b) James P. Sullivan	☐	☐

COMPANY NOMINEE UNOPPOSED BY LAND & BUILDINGS	**FOR**	**WITHHOLD**
a) Jay Paul Leupp	☐	☐

COMPANY NOMINEES OPPOSED BY LAND & BUILDINGS	**FOR**	**WITHHOLD**
a) Michael A. Stein	☐	☐
b) R. Dary Stone	☐	☐

LAND & BUILDINGS MAKES NO RECOMMENDATION WITH RESPECT TO PROPOSAL 2.

2. The Company's proposal to ratify the selection of Ernst & Young LLP to serve as the independent registered public accounting firm for the Company for the fiscal year ending December 31, 2022.

☐ FOR ☐ AGAINST ☐ ABSTAIN

LAND & BUILDINGS MAKES NO RECOMMENDATION WITH RESPECT TO PROPOSAL 3.

3. The Company's proposal to conduct an advisory vote on executive compensation.

☐ FOR ☐ AGAINST ☐ ABSTAIN

Figure 7. L&B Universal Proxy Card (reverse)

B. Historic Disincentives to Activism Via Proxy Contests

***Page 540.* Rename section title: The Evolving Proxy Contest Scene**

***Page 556.* Delete note 4 and replace with the following.**

In July 2020, the SEC amended Rule 14a-1(l) to codify the Commission's longstanding interpretation that proxy voting advice generally constitutes a "solicitation" subject to the proxy rules.[22] Proxy advice nevertheless will normally be exempt from compliance with the SEC proxy rules—other than the prohibition of fraud in Rule 14a-9—by Rule 14a-2(b)(2), which exempts solicitation of ten or fewer persons, and Rule 14a-2(b)(3).

The 2020 release also contained a number of amendments to Rules 14a-2 and 14a-9 designed to address the conflicts of interest and lack of transparency noted in Release 3052. In the wake of the 2020 Presidential election, however, the SEC shifted from a Republican to a Democratic majority. The new SEC leadership pushed through new rules repealing most of those provisions. As revised, however, Rule 14a-2(b)(9) retains a conflict-of-interest disclosure requirement:

> Paragraphs (b)(1) and (b)(3) of this section shall not be available to a person furnishing proxy voting advice covered by § 240.14a-1(l)(1)(iii)(A) ("proxy voting advice business") unless the proxy voting advice business includes in its proxy voting advice or in an electronic medium used to deliver the proxy voting advice prominent disclosure of:
>
> (i) Any information regarding an interest, transaction, or relationship of the proxy voting advice business (or its affiliates) that is material to assessing the objectivity of the proxy voting advice in light of the circumstances of the particular interest, transaction, or relationship; and
>
> (ii) Any policies and procedures used to identify, as well as the steps taken to address, any such material conflicts of interest arising from such interest, transaction, or relationship.

In addition, the SEC emphasized that a proxy advisory service could still "be liable under Rule 14a-9 for a material misstatement of fact, or an omission of material fact, including, depending on the facts and circumstances, with regard to its methodology, sources of information, or conflicts of interest."[23]

***Page 558.* Delete note 5.**

C. Defenses Against Proxy Contests

1. Basic Legal Standard

***Page 564.* Delete the *Blasius* opinion and all following materials in the section. Insert the following.**

***Coster v. UIP Companies, Inc.*, — A.3d —– (Del.2023)**

This appeal returns to the Supreme Court following remand. As the Court of Chancery recognized in its latest opinion, "[m]any aspects of the facts of this case were vexingly complicated or unique" and "the case gave rise to many close calls on which reasonable minds could differ."[2] We agree with the court's assessment and appreciate its work to address the issues remanded for reconsideration. We also agree with the court's observation that the dispute has been driven by hard feelings on both sides—the untimely death of Marion Coster's husband, Wout Coster, who could not secure his wife's

[22] Exemptions From the Proxy Rules for Proxy Voting Advice, Exchange Act Release No. 89,372 (July 22, 2020).
[23] Proxy Voting Advice, Exchange Act Release No. 95,266 (July 13, 2022).
[2] Coster v. UIP Cos., Inc., 2022 WL 1299127, at *14 (Del. Ch. May 2, 2022) [hereinafter *Coster II*].

financial security before his death, and the UIP board's desire to preserve UIP's operational viability after the loss of one of its major stockholders and founding members.*

. . .

I.

. . . UIP Companies, Inc. is a real estate services company founded in 2007 by Steven Schwat, Cornelius Bruggen, and Wout Coster ("Wout").The company operates through various subsidiaries that provide a range of services to investment properties in the Washington, D.C. area. Many of these properties are held in special purpose entities ("SPEs") that UIP owns alongside third-party investors.

Each of the three founders initially controlled a third of UIP's shares. In 2011, Bruggen left UIP and tendered his shares to the Company at no cost. This left Schwat and Wout as half owners of UIP.

In 2013, Wout notified Schwat and Peter Bonnell, a senior UIP executive, that he had been diagnosed with leukemia. Shortly after, the group began negotiations for a buyout in which Bonnell and Heath Wilkinson, another UIP executive, would purchase Wout's shares in the company. Bonnell had previously been promised equity in UIP on multiple occasions. As the prospect for promotion had stalled, Bonnell and Wilkinson had both considered leaving UIP. Therefore, beyond providing Wout with an exit, the buyout was also useful in incentivizing Bonnell and Wilkinson to stay.

Unfortunately, negotiations were unsuccessful. . . . Wout passed away on April 8, 2015, and his widow, Marion Coster ("Coster"), inherited his UIP interests.

Immediately after Wout's death, Schwat and Bonnell continued exploring buyout options with Coster. . . . Negotiations between the parties continued throughout 2016 and into 2017 as Coster sought an independent valuation of UIP.

A.

In August 2017, Coster provided UIP with a $7.3 million valuation and demanded to inspect UIP books and records. Coster followed up with a second inspection demand in October 2017. Then, "[a]fter much back and forth about the adequacy of the documents provided, on April 4, 2018, Coster called for a UIP stockholders special meeting to elect new board members."[15] At this time, UIP had a five-member board composed of Schwat, Bonnell, and Stephen Cox, UIP's Chief Financial Officer. Two seats were vacant due to Wout's passing and Cornelius Bruggen's departure in 2011.

The stockholder meeting took place on May 22, 2018. Coster, represented by counsel, raised multiple motions affecting the size and composition of the board. Predictably, each of Coster's motions failed due to Schwat's opposition. Later that day, the UIP board reduced the number of board seats to three through unanimous written consent.

A second stockholder meeting followed on June 4, 2018. The meeting also ended in deadlock as Schwat and Coster each opposed the other's respective motions. With the deadlock, Schwat, Bonnell, and Cox remained UIP's directors.

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* [Ed.: In a footnote to a portion of the text that has been omitted, the court explained that:

For those unfamiliar with the Delaware cases referred to in the opinion that now have shorthand references, Schnell refers to Schnell v. Chris-Craft Industries, Inc. 285 A.2d 437, 439 (Del. 1971), where Justice Herrmann famously wrote that "inequitable action does not become permissible simply because it is legally possible" and management cannot inequitably manipulate corporate machinery to perpetuate itself in office and disenfranchise the stockholders. Blasius refers to Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651, 659–61 (Del. Ch. 1988), where Chancellor Allen wrote that directors who interfere with board elections, even if in good faith, must have a compelling justification for their actions. And Unocal refers to Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985), where the Supreme Court used an enhanced standard of review to decide whether the directors "had reasonable grounds for believing that a danger to corporate policy and effectiveness existed" and that the board's response "was reasonable in relation to the threat posed."]

[15] [Coster v. UIP Cos., Inc., 255 A.3d 952, 956 (Del. 2021) (hereinafter *Coster Appellate Decision*)].

B.

Coster filed a complaint in the Court of Chancery seeking appointment of a custodian under 8 Del. C. § 226(a)(1) (the "Custodian Action").[16] Coster's "complaint mainly sought to impose a neutral tie-breaker to facilitate director elections, but it also lodged allegations against Schwat" about the lack of distributions and transparency into the company's affairs.[17] Coster "sought the appointment of a custodian with broad oversight and managerial powers."[18]

Coster's request for a "broadly empowered" custodian rather than one specifically tailored to target the stockholder deadlock "posed new risks to the Company."[19] As the Court of Chancery would later find, "[t]he appointment of a custodian with these powers would have given rise to broad termination rights in SPE contracts and threatened UIP's revenue stream, as UIP's business model is dependent on the continued viability of those contracts."[20] "Facing this threat to the Company," the UIP board decided to "issue the equity that they had long promised to Bonnell." Having conducted its own valuation that "valued a 100-percent, noncontrolling equity interest in UIP at $123,869," the UIP board offered, and Bonnell purchased, a one-third interest in the company for $41,289.67 (the "Stock Sale").[21]

The Stock Sale diluted Coster's ownership interest from one half to one third and negated her ability to block stockholder action as a half owner of the company. The Stock Sale also mooted the Custodian Action. Coster responded by filing suit and sought to cancel the Stock Sale.

C.

In its opinion following trial, the Court of Chancery upheld the Stock Sale under the entire fairness standard of review.[23] . . .

D.

In the first appeal, this Court did not disturb the Court of Chancery's entire fairness decision but remanded with instructions to review the Stock Sale under *Schnell* and *Blasius*. As explained in our first decision, while entire fairness is "Delaware's most onerous standard of review," it is "not [a] substitute for further equitable review" under *Schnell* or *Blasius* when the board interferes with director elections:

> In a vacuum, it might be that the price at which the board agreed to sell the one-third UIP equity interest to Bonnell was entirely fair, as was the process to set the price for the stock. But "inequitable action does not become permissible simply because it is legally

[16] 8 Del. C. § 226 allows for the Court of Chancery to appoint a custodian "upon application of any stockholder ... when ... [a]t any meeting held for the election of directors the stockholders are so divided that they have failed to elect successors to directors whose terms have expired or would have expired upon qualification of their successors."

[17] *Coster I*, at *10; *see* App. to Opening Br. at A94 ("[D]espite the apparent success of the Company in recent years, [Coster] has been denied any distributions from the Company since 2015, the year her husband, a founder, died. Over the same period, Mrs. Coster believes the current Chairman of the Board and President of the Company, Defendant Steven Schwat, has received a generous salary from the Company and is enjoying significant benefit from his 50% stake. Mr. Schwat has further prevented Mrs. Coster from gaining a meaningful view into the Company's financial affairs, and has barred her from any representation on the Board.").

[18] [Coster v. UIP Cos., Inc., 2020 WL 429906, at *10 (Del. Ch. Jan. 28, 2020), *rev'd*, 255 A.3d 952 (Del. 2021) (hereinafter *Coster I*)].

[19] *Coster II*, at *4.

[20] *Id.*

[21] *Id.* at 5.

[23] *Coster I*, at *12.

possible." If the board approved the Stock Sale for inequitable reasons, the Court of Chancery should have cancelled the Stock Sale. And if the board, acting in good faith, approved the Stock Sale for the "primary purpose of thwarting" Coster's vote to elect directors or reduce her leverage as an equal stockholder, it must "demonstrat[e] a compelling justification for such action" to withstand judicial scrutiny.

After remand, if the court decides that the board acted for inequitable purposes or in good faith but for the primary purpose of disenfranchisement without a compelling justification, it should cancel the Stock Sale and decide whether a custodian should be appointed for UIP.[25]

. . .

E.

On remand, the Court of Chancery found that the UIP board had not acted for inequitable purposes under *Schnell* and had compelling justifications for the Stock Sale under *Blasius*. . . . The court found that the threat posed by the Custodian Action was "an existential crisis" that justified the UIP board's actions and "that the Stock Sale was appropriately tailored to achieve the goal of mooting the Custodian Action while also achieving other important goals, such as implementing the succession plan that Wout favored and rewarding Bonnell."[34]

II.

In her second appeal, Coster has challenged the Court of Chancery's ruling on both remand questions. . . .

A.

. . . To frame our analysis, it is helpful to review again the circumstances of Schnell and Blasius. Both cases involved board action that interfered with director elections in contests for control—*Schnell*, a proxy solicitation, and *Blasius*, a consent solicitation.

In *Schnell*, the incumbent Chris-Craft board faced the prospect of a difficult proxy fight to retain their seats. In response to the threat to their tenure as board members, the board accelerated the annual meeting date and moved the meeting to a more remote location. The director defendants mounted no real defense to the Court of Chancery suit except to argue that their actions did not violate the Delaware General Corporation Law ("DGCL") or Chris-Craft's bylaws and were therefore legal. . . . On appeal, the Supreme Court took a dim view of the board's intentional efforts to obstruct the insurgent's proxy contest. As the Court held, even though the board's actions met all legal requirements, the Chris-Craft board was "attempt[ing] to utilize the corporate machinery and the Delaware Law for the purpose of perpetuating itself in office; and, to that [sic] end, for the purpose of obstructing legitimate efforts of dissident stockholders in the exercise of their rights to undertake a proxy contest against management."[39] In Justice Herrmann's oft-quoted words, "inequitable action does not become permissible simply because it is legally possible."[40] The Supreme Court ordered the Chris-Craft board to reinstate the original meeting date.

In *Blasius*, the Court of Chancery explored how *Schnell* operates in contested election cases, and specifically how *Schnell* was not the end of the road for judicial review of good faith board actions that interfered with director elections. Like *Schnell*, Blasius involved an incumbent board facing a consent solicitation aimed at replacing a majority of the board. Atlas Industries had a staggered board. Only

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[25] [*Coster Appellate Decision*] at 953–54 (quoting *Schnell*, 285 A.2d at 439 then quoting *Blasius*, 564 A.2d at 661–62).

[34] [*Coster II,*] at *12–13.
[39] [285 A.2d at 439.]
[40] *Id.*

seven of the authorized fifteen board seats were occupied. With a majority of stockholders behind the effort, an insurgent could in one action amend the company's bylaws, increase the board size to fifteen, and elect a new board majority of eight members.

If the Atlas board had acted on a clear day to establish new seats and to fill the vacancies, the circumstances would have been different. But for the Atlas board, the skies were cloudy, and it was raining. It faced a serious consent solicitation. In response, the board added two seats and filled the newly created positions with directors friendly to management. Now, Blasius had to win not one, but two elections to control the board.

. . .

Ultimately, Chancellor Allen concluded that, even if the board acted in good faith, it did not justify its interference with the stockholder franchise. The court did not propose to "invalidat[e], in equity, every board action taken for the sole or primary purpose of thwarting a shareholder vote."[53] But the board could not rely on the justification that it "knows better than do the shareholders what is in the corporation's best interest."[54]

B.

In the years since the Supreme Court and the Court of Chancery decided these iconic cases, . . . "[a]lmost all of the post-*Schnell* decisions involved situations where boards of directors deliberately employed various legal strategies either to frustrate or completely disenfranchise a shareholder vote."[57] [Accordingly], the Chancellor was correct in this case to cabin *Schnell* and its equitable review to those cases where the board acts within its legal power, but is motivated for selfish reasons to interfere with the stockholder franchise.

C.

. . .

Blasius [required] a board, even if acting in good faith, to demonstrate a "compelling justification" for interfering with the stockholder franchise. But another standard of review could also apply when the board interferes with the stockholder vote during a contest for control. In *Unocal Corporation v. Mesa Petroleum Company*, this Court noted [that when] stockholders challenge a board's use of anti-takeover measures, the board must show (i) that "they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed," and (ii) that the response was "reasonable in relation to the threat posed."[61] A defensive measure is an unreasonable response in relation to the threat if it is either draconian—coercive or preclusive—or falls outside a range of reasonable responses.[62]

In Stroud v. Grace, our Court first recognized how both *Blasius* and *Unocal* review were called for in a proxy fight involving a tender offer:

> Board action interfering with the exercise of the franchise often arose during a hostile contest for control where an acquiror launched both a proxy fight and a tender offer. Such action necessarily invoked both Unocal and Blasius. We note that the two "tests" are not

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[53] [*Blasius*, 564 A.2d] at 662.

[54] *Id.* at 663; *see also* Stahl v. Apple Bancorp, Inc., 579 A.2d 1115, 1124 (Del. Ch. 1990) (rejecting "the notion that the prospect that the shareholders might vote differently than the board recommends can alone constitute any threat to a corporate interest").

[57] Stroud v. Grace, 606 A.2d 75, 91 (Del. 1992).

[61] [493 A.2d] at 955.

[62] *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1367 (Del. 1995).

mutually exclusive because both recognize the inherent conflicts of interest that arise when shareholders are not permitted free exercise of their franchise. . . .[63]

. . .

In MM Companies v. Liquid Audio, Inc., . . . the Supreme Court applied *Blasius* "within *Unocal*" as the standard of review:

> When the primary purpose of a board of directors' defensive measure is to interfere with or impede the effective exercise of the shareholder franchise in a contested election for directors, the board must first demonstrate a compelling justification for such action as a condition precedent to any judicial consideration of reasonableness and proportionately.... To invoke the Blasius compelling justification standard of review within an application of the Unocal standard of review, the defensive actions of the board only need to be taken for the primary purpose of interfering with or impeding the effectiveness of the stockholder vote in a contested election for directors.[68]

Even though the Supreme Court in *Liquid Audio* combined *Blasius* and *Unocal* review, it did not solve the practical problem of how to turn *Unocal's* reasonableness review and *Blasius*' "primary purpose" and "compelling justification" elements into a useful standard of review. The *Blasius* "compelling justification" standard of review turned out to be unworkable in practice. Once the court required a compelling justification to justify the board's action, the outcome was, for the most part, preordained.[69] The Court of Chancery also skirted *Blasius* review by limiting the "primary purpose" requirement and redefining what it meant to be compelling.

. . .

D.

In *Unocal*, the Supreme Court remarked that "our corporate law is not static."[88] Experience has shown that *Schnell* and *Blasius* review, as a matter of precedent and practice, have been and can be folded into *Unocal* review to accomplish the same ends—enhanced judicial scrutiny of board action that interferes with a corporate election or a stockholder's voting rights in contests for control. When *Unocal* is applied in this context, it can "subsume[ ] the question of loyalty that pervades all fiduciary duty cases, which is whether the directors have acted for proper reasons" and "thus address[ ] issues of good faith such as were at stake in *Schnell*."[90] *Unocal* can also be applied with the sensitivity *Blasius* review brings to protect the fundamental interests at stake—the free exercise of the stockholder vote as an essential element of corporate democracy.

. . . When a stockholder challenges board action that interferes with the election of directors or a stockholder vote in a contest for corporate control, the board bears the burden of proof. First, the court should review whether the board faced a threat "to an important corporate interest or to the achievement of a significant corporate benefit." The threat must be real and not pretextual, and the board's motivations must be proper and not selfish or disloyal. As Chancellor Allen stated long ago,

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[63] *Stroud*, 606 A.2d at 92 n.3 (internal citations omitted); *see also Unitrin*, 651 A.2d at 1379–80 (noting use of *Blasius* and *Unocal* in contests for corporate control).

[68] [MM Cos. v. Liquid Audio, Inc., 813 A.2d 1118, 1132 (Del. 2003).]

[69] *See* [Chesapeake Corp. v. Shore, 771 A.2d 293, 323 (Del. Ch. 2000)] ("In reality, invocation of the *Blasius* standard of review usually signals that the court will invalidate the board action under examination. Failure to invoke *Blasius*, conversely, typically indicates that the board action survived (or will survive) review under Unocal."); William T. Allen et. al., *Function over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 56 BUS. LAW. 1287, 1314 (2001) ("[T]he post-*Blasius* decisions surfaced the reality that a sorting mechanism was needed to insulate from the severe 'compelling justification' test, situations where directors took direct action to influence the electoral process, but in a manner that was consistent with their legitimate authority. ... The elements of the *Unocal/Unitrin* analysis therefore gave courts the tool to answer the predicate question to the application of *Blasius*—did the directors act with the primary purpose of disenfranchisement?").

[88] 493 A.2d at 957.

[90] [Mercier v. Inter-Tel (Del.), Inc., 929 A.2d 786, 807 (Del. Ch. 2007).]

the threat cannot be justified on the grounds that the board knows what is in the best interests of the stockholders.

Second, the court should review whether the board's response to the threat was reasonable in relation to the threat posed and was not preclusive or coercive to the stockholder franchise. To guard against unwarranted interference with corporate elections or stockholder votes in contests for corporate control, a board that is properly motivated and has identified a legitimate threat must tailor its response to only what is necessary to counter the threat. The board's response to the threat cannot deprive the stockholders of a vote or coerce the stockholders to vote a particular way.

Applying Unocal review in this case with sensitivity to the stockholder franchise is no stretch for our law. . . .

E.

In our first decision, we highlighted facts in the Court of Chancery's first decision that might have led to the conclusion that the board acted for selfish reasons. But we recognized that the court had made findings inconsistent with this result and remanded to allow the Court of Chancery to reconsider its decision in light of our first opinion. On remand the court did as requested. The court found that there was "more to the story" than contained in its first opinion.[98] It supplemented the earlier factual findings with the following:

- "Without making any meaningful effort to negotiate board composition, Plaintiff filed a complaint in this Court seeking the appointment of a custodian;"
- "Plaintiff's request for custodial relief was extremely broad. Plaintiff did not present a tailored request for relief that targeted the stockholder deadlock. Rather, she asked the court to empower a custodian to 'exercise full authority and control over the Company, its operations, and management;'"
- "The threat of a court-appointed custodian so broadly empowered posed new risks to the Company. The appointment of a custodian with these powers would have given rise to broad termination rights in SPE contracts and threatened UIP's revenue stream, as UIP's business model is dependent on the continued viability of those contracts;"
- "Facing this threat to the Company," the UIP board "identified a solution" to issue equity "long promised to Bonnell" that "implent[ed] a succession plan" proposed "on a clear day;"
- The Stock Sale would "moot the Custodian Action and eliminate the risks the appointment of a custodian posed to UIP" and would "eliminate the stockholder leverage that Plaintiff was using to try to force a buyout at a price detrimental to the Company;"
- The UIP board's motives were not "pretexts for entrenchment for selfish reasons" or "post-hoc justifications;" and
- "[T]hese were genuine motivations for their actions that stood alongside the more problematic purposes that [Coster I] identified and the Appellate Decision collected."

After its additional fact findings, the Court of Chancery gathered the many strands of precedent and conducted a careful review of the UIP board's actions. The Chancellor found that the UIP board faced a threat—which the court described as an "existential crisis"—to UIP's existence through a deadlocked stockholder vote and the risk of a custodian appointment. Although the court thought that some of the board's reasons for approving the Stock Sale were problematic, on balance the court held that the board was properly motivated in responding to the threat. According to the court, the UIP board acted in good faith "to advance the best interests of UIP" by "reward[ing] and retain[ing] an essential employee," "implement[ing] a succession plan that Wout had favored," and "moot[ing] the Custodian Action to avoid risk of default under key contracts."[106] The court also relied on its earlier finding that the UIP board issued UIP stock to Bonnell at an entirely fair price.

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[98] *Coster II*, at *3.
[106] *Id*. at *10.

The Court of Chancery also found that the UIP board responded reasonably and proportionately to the threat posed when it approved the Stock Sale and mooted the Custodian Action. As it held, "in the exceptionally unique circumstances of this case," without the Stock Sale, the possibility that a custodian appointed with broad powers would jeopardize key contracts caused an existential crisis at UIP. The Stock Sale, the court held, "was appropriately tailored to achieve the goal of mooting the Custodian Action" while implementing the succession plan and retaining Bonnell.[108] And the court noted that there were more aggressive options that could have been, but were not, pursued to break the deadlock.

*Finally, the board's response to the existential threat posed by the stockholder deadlock and custodian action was not preclusive or coercive. Although the Stock Sale effectively foreclosed Coster from perpetuating the deadlock facing UIP, the new three-way ownership of the company presented a potentially more effective way for her to exercise actual control. As the Court of Chancery noted, Schwat and Bonnell are not bound to vote together, meaning Coster could cast a swing vote at stockholder meetings.[110] As an equal one third owner with the two other stockholders, Coster can join forces with either one of UIP's other owners "at some point in the future."[111]A realistic path to control of UIP negates the preclusive impact of the Stock Sale.

. . .

III.

The judgment of the Court of Chancery is affirmed.

Notes and questions

1. If the case had been decided under the original *Blasius* compelling justification standard, what would the result have been?

2. What does the court mean by its reference to "clear day" actions? How would such actions be analyzed?

3. When does the *Coster* standard apply rather than the business judgment rule?

4. Given the apparent ability of courts to use the *Schnell* doctrine to police incumbent interference with the shareholder franchise, is the *Coster* standard necessary?

5. In *Coalition to Advocate Public Utility Responsibility, Inc. v. Engels*,[24] the directors of Northern States Power Company (referred to by the court as N.S.P.) tried to manipulate the corporation's bylaws to prevent an insurgent director candidate—one Alpha Smaby[25]—from being elected:

> 4) N.S.P. has historically elected Directors each year for a one-year term. In February of 1973, there were 14 Directors. At the Board of Directors' meeting of February 28, 1973, the Board of Directors considered in detail a proposed draft proxy soliciting

[108] *Id*. at *11–12.

[110] *See Coster II,* at *13 ("Bonnell could switch sides tomorrow and unite with Plaintiff to Schwat's detriment. The record reflects that Schwat and Bonnell have disagreed on a number of business decisions").

[111] Air Prod. & Chemicals, Inc. v. Airgas, Inc., 16 A.3d 48, 115 (Del. Ch. 2011).

[24] 364 F. Supp. 1202 (D. Minn. 1973)

[25] According to Wikipedia:

> Alpha Sunde Smaby (February 11, 1910–July 18, 1991) was an American politician and teacher.
>
> Born in Sacred Heart, Minnesota, Smaby graduated from University of Minnesota and Winona State University. She then taught school and then worked for Cargill, Inc. Smaby served in the Minnesota House of Representatives from 1965 until 1969 and was a Democrat. During the 1968 United States Presidential campaign, Smaby was a delegate to the Democratic Party Convention and supported United States Senator Eugene McCarthy. Smaby died of cancer in Saint Paul, Minnesota.

Alpha Sunde Smaby, https://en.wikipedia.org/w/index.php?title=Alpha_Sunde_Smaby (last visited July 25, 2017).

statement which contemplated the continuation of the 14 member Board. These draft materials made direct and substantial reference to Alpha Smaby and urged the shareholders to reject her candidacy. . . .

6) Subsequent to the February meeting, the exact date is not known at this time, it was decided by the Directors of N.S.P. to reduce the number of Directors from 14 to 12 and to classify the Directors in groups of four for election to staggered terms of one, two and three years. Without the changes, just over 7% of the vote would be sufficient to elect one Director under the cumulative voting provision, but after the changes about 20% of the vote would be required. There was good reason to believe that Alpha Smaby might control up to 9% of the voting shares. Although the above changes were not formally approved by the Board of Directors until a special meeting was called on March 27, 1973, the proposed changes were submitted to the SEC approximately one week prior to the Board's formal approval.

7) N.S.P. candidly admits that such changes were not proposed because of long-term business considerations but that the changes were specifically aimed at the candidacy of Alpha Smaby. It is clear to the Court that the changes were instigated in an attempt to make her effort to win a seat on the Board more difficult and, in fact, were done to frustrate her efforts.

. . .

Plaintiffs concede that the actions of the defendants do not violate any state statutory law but argue that the manipulation of the corporate machinery by insiders for the sole purpose of frustrating the candidacy of a minority shareholder . . . is a breach of the insiders' fiduciary duty to the minority shareholders. Plaintiffs rely heavily on . . . Delaware cases which basically stand for the proposition that actions by insiders, although otherwise lawful, may be enjoined if they act to injure the rights of minority shareholders. In [*Schnell v. Chris-Craft Industries*, 285 A.2d 437 (Del.Supr.1971),] the Delaware Supreme Court held that management's efforts to use the corporate machinery and Delaware law for the purpose of perpetrating itself in office and obstructing legitimate efforts of the dissident stockholders in the exercise of their rights to undertake a proxy contest against management was impermissible. The insiders had advanced the date of the stockholders' meeting in an effort to frustrate the efforts of minority shareholders who desired to wage a proxy contest. The actions of the insiders were enjoined despite the fact that they were in compliance with the company by-laws and applicable Delaware law. The basis for these opinions rests on the fiduciary duty imposed on Directors and Officers of a corporation to deal fairly and justly with the corporation and all of its shareholders including minority shareholders. The Officers and Directors of N.S.P. are in a fiduciary relationship with the minority shareholders and as such owe them a duty to deal with them fairly and in good faith.

In the instant case, the actions of the insiders, if not unfair, were certainly questionable in light of their fiduciary obligation to the plaintiff shareholders. Not only did the defendants change the rules in the middle of the game, but they refused to disclose the existence of the changes when approached by the plaintiffs. Both of these actions served to frustrate the plaintiff shareholders' legitimate efforts to run for the Board of Directors and may well be a breach of fiduciary duty. . . .

Both of the changes made by the N.S.P. board were permitted by statute. So why did the court invalidate them? Would the *Blasius* court have reached the same result? Would the *Coster* court have reached the same result?

Suppose that one month after the 1973 annual shareholder meeting the N.S.P. board amended the company's bylaws to effect a reduction in the number of directors and to classify the board effective with the 1974 annual shareholder meeting. Would the court enjoin those changes? Would the *Blasius* court have enjoined those changes? Would the *Coster* court have enjoined those changes?

6. In *Portnoy v. Cryo-Cell Int'l, Inc.*,[26] the incumbent directors feared losing a proxy contest and took a variety of steps intended to ensure their victory. One of those steps involved a deal pursuant to which a large shareholder—one Andrew Filipowski—agreed to support the incumbent board provided that the board would include the shareholder on its slate of candidates and—if successful in winning the proxy contest—would increase the number of board members from six to seven and appoint a crony of the shareholder to fill the resulting vacancy. Then Vice Chancellor Leo Strine explained that:

> As defined by Vice Chancellor Hartnett in his important decision in *Schreiber v. Carney*, "[v]ote-buying . . . is simply a voting agreement supported by consideration personal to the stockholder, whereby the stockholder divorces his discretionary voting power and votes as directed by the offeror." . . .
>
> To say that the law of corporations has struggled with how to address the subject of so-called "vote buying" is no insult to judges or corporate law scholars, the question of what inducements and agreements may legitimately be forged to cement a voting coalition is doubtless as old as the concept of a polity itself. For these very real-world reasons, *Schreiber* refused to say that any sort of arrangement involving the exchange of consideration in connection with a stockholder's agreement to vote a particular way was forbidden vote buying. Indeed, distinguished scholars have anguished (the adjective I take away from their work) over how to deal with such arrangements, with most concluding that flat-out prohibitions are neither workable nor of utility to diversified stockholders. . . .
>
> To deal with these complexities, *Schreiber* declined to find that vote buying was, in the first instance, per se improper. Rather, *Schreiber* articulated a two-pronged analysis. In the first instance, if the plaintiff can show that the "object or purpose [of the vote buying was] to defraud or in some way disenfranchise the other stockholders," the arrangement would be "illegal per se." Putting this in terms that I think are truer to the way our corporate law works, what I take from this is that if the plaintiff proved that the arrangement under challenge was improperly motivated, then the arrangement would be set aside in equity, irrespective of its technical compliance with the DGCL.[157] That is, in keeping with the traditional vigilance this court has displayed in ensuring the fairness of the corporate election process, and in particular the process by which directors are elected, purposely inequitable conduct in the accumulation of voting power will not be tolerated. Even when a vote buying arrangement cannot be found, in the first instance, to be motivated by a fraudulent, disenfranchising, or otherwise inequitable intent, *Schreiber* concluded that "because vote-buying is so easily susceptible of abuse it must be viewed as a voidable transaction subject to a test for intrinsic fairness."
>
> Subjecting an agreement to add a potential insurgent to a management slate to the *Schreiber* intrinsic fairness test would, in my view, be an inadvisable and counterproductive precedent. If one takes a judicial standard of review seriously, as the members of this court do, the decision to subject all such arrangements to the entire fairness standard could result in creating litigable factual issues about a large number of useful compromises that result in the addition of fresh blood to management slates, new candidates who will tend to represent actual owners of equity and might therefore be more independent of management and more useful representatives of the interests of stockholders generally. . . .
>
> . . . If the only arrangement at issue is a promise to add a potential insurgent to the management slate in exchange for the insurgent's voting support, then the arrangement is subject to stockholder policing in an obvious, but nonetheless, potent form. That policing occurs at the ballot box itself.

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[26] 940 A.2d 43 (Del. Ch. 2008).

[157] See Schnell v. Chris-Craft Indus., Inc., 285 A.2d 437, 439 (Del.1971) (holding that "inequitable action does not become permissible simply because it is legally possible") . . . .

> Here, to be specific, the Cryo-Cell stockholders went to the polls knowing that Filipowski had been added to the Management Slate. Those stockholders also knew that Filipowski had contracted to vote the Filipowski Group's shares for the Management Slate. Although it was not publicly disclosed that Filipowski's agreement to vote for the Management Slate had been conditioned on his addition to that Slate, and that the incumbents had added Filipowski to the Management Slate in exchange for his support, that inference was, I think, unmistakable to any rational stockholder. . . .
>
> In expressing concerns about over-breadth in this area, this decision echoes concerns voiced by the Supreme Court and this court about the difficulty of applying the compelling justification test articulated in *Blasius* in a manner that works sensible results.[162] But like those decisions, this decision is rooted in the premise that the *Schnell* doctrine, authorizing this court to set aside conduct that is inequitably motivated and that unfairly tilts the electoral playing field, is itself a potent tool of equity.

Why shouldn't *Blasius* apply to vote buying? If *Blasius* had been applied, what compelling justification—if any—could the incumbent board have put forward to justify the deal with Filipowski?

Would *Coster* apply to vote buying? If *Coster* had been applied, what arguments could the incumbent board have put forward to justify the deal with Filipowski?

Strine's opinion in *Portnoy* can be seen as part of a larger trend in Delaware corporate law towards judicial deference to informed, non-coerced shareholder votes. The leading example of that trend is *Corwin v. KKR Financial Holdings LLC*,[27] in which the Delaware Supreme Court held that the business judgment rule was the proper standard of review for a merger between a target corporation and a minority shareholder that was approved by a fully informed, non-coerced vote of the disinterested shareholders. "When the real parties in interest—the disinterested equity owners—can easily protect themselves at the ballot box by simply voting no, the utility of a litigation-intrusive standard of review promises more costs to stockholders in the form of litigation rents and inhibitions on risk taking than it promises in terms of benefits to them." Put another way, *Corwin* posits that informed, disinterested, non-coerced shareholders—rather than plaintiffs' lawyers or courts—should have the last word on the merits of a transaction.

7. Some courts have suggested that *Blasius* should be limited to proxy contests involving director elections:

> *Blasius* anticipates a defensive measure in response to a threat to corporate control. Beyond this, its application has been largely limited to disputes over the election of directors. Accordingly, "courts will apply the exacting *Blasius* standard sparingly, and only in circumstances in which self-interested or faithless fiduciaries act to deprive stockholders of a full and fair opportunity to participate in the matter." Of particular significance here, "the reasoning of *Blasius* is far less powerful when the matter up for consideration has little or no bearing on whether the directors will continue in office."[28]

Is there a good reason for not applying *Coster* to issue contests?

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[162] See, e.g., Williams v. Geier, 671 A.2d 1368, 1376 (Del.1996) ("Blasius' burden of demonstrating a 'compelling justification' is quite onerous, and is therefore applied rarely.") . . . .

[27] 125 A.3d 304 (Del. 2015).

[28] In re Bear Stearns Litig., 870 N.Y.S.2d 709, 733 (N.Y. Sup. 2008) (citations and footnote omitted).

Chapter 12. Shareholder Activism via Proposals

A. Rule 14a–8

***Page 607*: Delete existing two paragraphs following the heading and replace with the following.**

Under Rule 14a–8(b)(1), a proponent must have continuously held at least: $2,000 of the company's securities entitled to vote on the proposal for at least three years; $15,000 of the company's securities entitled to vote on the proposal for at least two years; or $25,000 of the company's securities entitled to vote on the proposal for at least one year. What happens if the individual shareholder cannot satisfy these requirements? (1) Suppose three shareholders want to jointly support a proposal: A, who has owned $800 in stock for 2 years; B, who has owned $900 in stock for 18 months; and C, who has owned $500 in stock for 13 months. (2) D and E want to sponsor a separate proposal. D has owned $1200 in stock for two years; E has owned $1200 in stock for two months. Can they aggregate their holdings for purposes of meeting either the dollar threshold or the holding period? No. Although the Rule allows groups of shareholders to jointly sponsor a proposal, each member of the group must individually satisfy both the dollar threshold and the holding period.

***Page 608*: Delete first three paragraphs under this heading and replace with the following.**

Number of Submissions. Per Rule 14a–8(c), the proponent may only submit one proposal per corporation per year.[29] There is no limit to the number of companies to which a proponent can submit proposals in a given year, however. As long as the proponent meets the eligibility requirements for each firm, an activist thus may press the same proposal at multiple firms. As noted below, however, either the proponent or a representative of the proponent must attend each meeting at which the proposal is put to a vote.[30]

Prior Submissions. The proponent may submit a proposal that "addresses substantially the same subject matter as a proposal, or proposals, previously included in the company's proxy materials within the preceding five calendar years" but only if the prior proposal or proposals a specified level of support. A resubmitted proposal thus must be included if it was submitted: (i) once during the preceding five years and received 5% or more of the vote; (ii) twice in the preceding five years and received 15% or more of the vote the last time it was submitted; or (iii) 3 or more times in the preceding five years and received 25% or more of the vote the last time it was submitted.[31]

In July 2022, the SEC proposed an amendment to Rule 14a-8(i)(12) that would permit exclusion only of proposals that "substantially duplicates" the earlier proposals. According to the SEC, this standard requires a proposal to address "the same subject matter" and seek "the same objective by the same means" as a previously submitted proposal.[32]

Attendance. Although the proxy system generally is designed to facilitate participation by shareholders who choose not to attend the shareholders' meeting, the shareholder proposal rule requires the proponent or a representative to present the proposal in person at the meeting. If the proponent fails to show up, Rule 14a-8(h) bars the proponent from using the rule at that company for the following two years.

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[29] A shareholder-proponent may not submit one proposal in his or her own name and simultaneously serve as a representative to submit a different proposal on another shareholder's behalf for consideration at the same meeting.

[30] A representative may not submit more than one proposal to be considered at the same meeting, even if the representative were to submit each proposal on behalf of different shareholders.

[31] Rule 14a–8(i)(12).

[32] Substantial Implementation, Duplication, and Resubmission of Shareholder Proposals Under Exchange Act Rule 14a-8, Exchange Act Release No. 95,267 (July 13, 2022).

C. Management Resistance to Proposals: Grounds for Excluding a Proposal

***Page 628*. Insert new note 1 and renumber the other notes accordingly**.

In 2021, the SEC staff released interpretative guidance confirming its "longstanding approach . . . of analyzing Rule 14a-8(i)(5) in a manner we believe is consistent with *Lovenheim* . . .. As a result, . . . proposals that raise issues of broad social or ethical concern related to the company's business may not be excluded, even if the relevant business falls below the economic thresholds of Rule 14a-8(i)(5)."[33]

***Page 643*. Add the following to the end of note 2**.

In 2021, the SEC staff issued interpretative guidance explaining that in responding to no-action requests the staff "will not focus on determining the nexus between a policy issue and the company, but will instead focus on the social policy significance of the issue that is the subject of the shareholder proposal. In making this determination, the staff will consider whether the proposal raises issues with a broad societal impact, such that they transcend the ordinary business of the company."[34] As an example of the type of proposal that would not be excludable under this guidance, the staff stated that "proposals squarely raising human capital management issues with a broad societal impact would not be subject to exclusion solely because the proponent did not demonstrate that the human capital management issue was significant to the company."[35]

What the guidance left unclear was whether a proposal raising a matter that has social significance but utterly lacking any nexus with the company's business would be excludable under Rule 14a-8(i)(7). In other words, does the SEC accept that a proposal must "bear on" the company's business? In any case, recall that a proposal lacking such a nexus should be excludable under Rule 14a-8(i)(5).

***Page 644*. Insert new note 8 and renumber the remaining notes accordingly**.

8. The SEC staff's 2021 interpretative guidance confirmed that proposals seeking to micromanage the company may be excluded under Rule 14a-8(i)(7). On the other hand, the staff opined that "proposals seeking detail or seeking to promote timeframes or methods do not per se constitute micromanagement. . . . This approach is consistent with the Commission's views on the ordinary business exclusion, which is designed to preserve management's discretion on ordinary business matters but not prevent shareholders from providing high-level direction on large strategic corporate matters."[36] The staff explained that:

> Our recent letter to ConocoPhillips Company provides an example of our current approach to micromanagement. In that letter the staff denied no-action relief for a proposal requesting that the company set targets covering the greenhouse gas emissions of the company's operations and products. The proposal requested that the company set emission reduction targets and it did not impose a specific method for doing so. The staff concluded this proposal did not micromanage to such a degree to justify exclusion under Rule 14a-8(i)(7).[37]

[33] SEC Division of Corporation Finance, Shareholder Proposals: Staff Legal Bulletin No. 14L (CF) (Nov. 3, 2021).
[34] SEC Division of Corporation Finance, Shareholder Proposals: Staff Legal Bulletin No. 14L (CF) (Nov. 3, 2021).
[35] Id.
[36] SEC Division of Corporation Finance, Shareholder Proposals: Staff Legal Bulletin No. 14L (CF) (Nov. 3, 2021).
[37] Id.