

CLIENT ALERT

SEC Proposes Amendments to Rules Governing Proxy Voting Advice and Adopts Rules Regarding Universal Proxy Cards

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Amendments to Rules Governing Proxy Voting Advice

On November 17, 2021, the Securities and Exchange Commission (the “SEC” or the “Commission”) voted 3-2 to propose amendments to the rules governing proxy voting advice that were enacted last year.¹ Below is brief history of the prior rulemaking in this area and a summary of the proposed amendments.

Prior Developments

On August 21, 2019, the SEC issued an interpretation affirming its long-standing view that proxy voting advice provided by proxy advisory firms generally constitutes a “solicitation” under the federal proxy rules (the “2019 Guidance”).²

¹ See Proxy Voting Advice, Securities Exchange Act of 1934 (the “Exchange Act”) Release No. 93595 (Nov. 17, 2021).

² See Commission Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice, Exchange Act Release No. 86721 (Aug. 21, 2019).

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On November 5, 2019, the SEC issued proposed amendments to its rules governing proxy voting advice provided by proxy advisory firms.³

On July 22, 2020, the SEC voted 3-2 to adopt final rules regarding proxy voting advice provided by proxy advisory firms (the “2020 Final Rules”).⁴ The 2020 Final Rules, among other things:

- Amended Rule 14a-1(1) under the Exchange Act to codify the SEC’s interpretation that proxy voting advice generally constitutes a “solicitation” subject to the federal proxy rules;
- Adopted Rule 14a-2(b)(9) under the Exchange Act to add two new conditions that each proxy advisory firm would generally need to satisfy to avoid certain other proxy requirements. The conditions include:
 - (i) a conflicts of interest disclosure requirement; and
 - (ii) a requirement to adopt and disclose written policies reasonably designed to ensure that (A) each applicable issuer has the proxy voting advice of such proxy advisory firm available to it at the same time or prior to the time such advice is disseminated to clients of the proxy advisory firm and (B) the proxy advisory firm provides its clients with a mechanism (such as a hyperlink) by which they can be expected to become aware of any written statements by the applicable issuer regarding the proxy voting advice before the shareholders’ meeting (collectively, the “Rule 14a-2 Conditions”); and
- Added a new Note (e) to Exchange Act Rule 14a-9, which prohibits false and misleading statements, to include specific examples of material misstatements or omissions related to proxy voting advice.

The amendments to Rules 14a-1(1) and 14a-9 became effective on November 2, 2020 and the Rule 14a-2 Conditions are set to become effective on December 1, 2021. One market-leading proxy advisory firm has filed a lawsuit against the SEC challenging the 2020 Final Rules. The suit is currently being held in abeyance.

Earlier this year, SEC Chair Gary Gensler directed Staff from the Division of Corporation Finance to consider whether to recommend further regulatory action regarding proxy voting advice. Subsequently, on June 1, 2021, Staff from the Division of Corporation Finance issued a statement (the “CF Statement”) providing that, pending further regulatory action

³ See Amendments to Exemptions From the Proxy Rules for Proxy Voting Advice, Exchange Act Release No. 87457 (Nov. 5, 2019).

⁴ See Exemptions From the Proxy Rules for Proxy Voting Advice, Exchange Act Release No. 89372 (July 22, 2020).

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by the SEC, the Staff would not recommend that the Commission take enforcement actions based on the 2020 Final Rules or the 2019 Guidance.⁵

On October 13, 2021, the National Association of Manufacturers and Natural Gas Services Group, Inc. filed a lawsuit as to the CF Statement. The lawsuit argues that the Administrative Procedure Act requires the SEC to engage in notice-and-comment rulemaking whenever it amends a regulation, including when it desires to suspend the regulation's effectiveness.⁶

Proposed Rule Amendments

On November 17, 2021, the SEC voted 3-2 to propose rules partially amending the 2020 Final Rules (the "2021 Proposed Amendments"). The 2021 Proposed Amendments would remove the Rule 14a-2 Conditions and remove Note (e) to Rule 14a-9. The conflicts of interest disclosure requirement would still be in effect and proxy voting advice would remain a solicitation subject to the federal proxy rules.

Court challenges to the amendments are likely when the notice-and-comment rulemaking process is complete and final rules are issued. In any such court proceeding, the Commission will be required to show that there are "good reasons" for the changes to the 2020 Final Rules.⁷

In connection with the notice-and-comment rulemaking process for the 2020 Final Rules, the Commission made adjustments to the then proposed rules based on investor comments. As to the removal of the Rule 14a-2 Conditions, the proposing release for the 2021 Proposed Amendments (the "Proposing Release") notes that many investors still have strong concerns about the Rule 14a-2 Conditions. The Proposing Release also notes that most of the major proxy advisory firms have current practices that could address some of the concerns underlying the Rule 14a-2 Conditions, including the existence of a Best Practices Principles Group comprised of most of the major proxy advisory firms. However, the Proposing Release does note that many of the mechanisms of the Best Practices Principles Group were in place and considered by the Commission at the time it adopted the 2020 Final Rules.

Commissioner Peirce issued a statement in dissent, noting that (i) the Commission considered concerns raised by all commenters during the rulemaking process and the Proposing Release fails to identify any new concerns, and (ii) the Commission was well aware of the Best Practices Principles Group during the prior rulemaking process.⁸

⁵ See Statement on Compliance with the Commission's 2019 Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice and Amended Rules 14(a)-1(1), 14(a)-2(b), 14(a)-9, Division of Corporation Finance (June 1, 2021).

⁶ See National Association of Manufacturers et al. v. SEC, No. 7:21-cv-183 (W.D. Tex.).

⁷ Todd Garvey, A Brief Overview of Rulemaking and Judicial Review, Congressional Research Service (Mar. 27, 2017).

⁸ See Dissenting Statement on Proxy Voting Advice Proposal, Commissioner Hester Peirce (Nov. 17, 2021).

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As to the removal of note (e) to Rule 14a-9, the Proposing Release notes a concern by proxy advisory firms regarding the extent of their liability under Rule 14a-9 for disagreements between proxy advisory firms and issuers. In the adopting release for the 2020 Final Rules, the Commission had stated that the amendments do not make “mere differences of opinion” actionable under Rule 14a-9.

Comments on the 2021 Proposed Amendments must be received within 30 days after the Proposing Release is published in the Federal Register.

Universal Proxy Cards

Also on November 17, 2021, the Commission voted 4-1 to issue final rules (the “Final Universal Proxy Rules”) requiring the use of a universal proxy card in all non-exempt solicitations involving director election contests, except those involving registered investment companies and business development companies.⁹ The rules also made certain other changes to the federal proxy rules relating to the adoption of a universal proxy requirement. The universal proxy card will be required to include the names of all duly nominated director candidates presented for election by any party.

As noted in the adopting release for the Final Universal Proxy Rules (the “Adopting Release”), the current proxy rules do not allow a shareholder voting by proxy in a contested election to replicate the vote they could cast if they voted in person at a shareholder meeting. Shareholders voting in person may select among all of the duly nominated director candidates proposed by any party in a contested election, and vote for any combination of candidates. However, shareholders voting by proxy historically have not had the same flexibility due to the interplay between state and federal law, and thus have generally been forced to choose between the proxy card of the company or of the dissident.

In 2016, the Commission proposed rule amendments to mandate the use of universal proxy cards in contested director elections to allow shareholders to vote by proxy in the same manner as they could if they attended a shareholder meeting.¹⁰ Earlier this year the Commission reopened the comment period for the proposing release, and this week the Commission adopted the proposed rules substantially as proposed except for an increase in the minimum solicitation requirement.

The Final Universal Proxy Rules include a requirement that dissidents must solicit the holders of shares representing at least 67% of the voting power of the shares entitled to vote at the meeting (up from a majority in the proposing release). The Adopting Release notes that this requirement was intended to strike the appropriate balance to ensure that dissidents must still engage in meaningful independent solicitation efforts in order to have their director nominees elected.

⁹ See Universal Proxy, Exchange Act Release No. 93596 (Nov. 17, 2021).

¹⁰ See Universal Proxy, Exchange Act Release No. 79164 (Oct. 26, 2016).

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There is no requirement as to the size of a dissident's equity position in the company or the length of time it has held such position. Commissioners Peirce and Roisman each issued a statement noting that they would have preferred the Final Universal Proxy Rules contain ownership requirements similar to those for shareholders who desire to introduce a proposal for a company meeting.¹¹ The Adopting Release noted these concerns but concluded that a universal proxy requirement should not be dependent on these ownership requirements as the purpose of the rule is to allow shareholders to exercise their right to vote for directors in the same manner as they could if they attended the meeting in-person.

The effective date for the Final Universal Proxy Rules is 30 days after the Adopting Release is published in the Federal Register.

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¹¹ See Dissenting Statement on Universal Proxy, Commissioner Hester Peirce (Nov. 17, 2021); Statement on Universal Proxy Rules, Commissioner Elad Roisman (Nov. 17, 2021).