

November 18, 2021

SEC Mandates Universal Proxy Cards in Contested Director Elections

SUMMARY

On November 17, 2021, the Securities and Exchange Commission adopted rules mandating universal proxy cards in contested director elections. The new rules will require issuers and dissidents to use proxy cards that list the names of both the issuer's and dissident's nominees, allowing shareholders to select among all nominees in a manner designed to more closely mirror in-person voting practices. In addition, the new rules require dissidents to solicit holders of a minimum of 67 percent of the voting power of shares entitled to vote in the election. The new rules also establish notice, filing and presentation requirements when using a universal proxy card. The new rules are scheduled to take effect for contested elections after August 31, 2022. The final rules can be found [here](#).

The new rules were adopted by a 4-to-1 vote, with the approving Commissioners and SEC staff noting that the adopted rules address the asymmetry between in-person voting and proxy voting.

BACKGROUND

A. CURRENT PROXY CONTEST PRACTICE

Under the current proxy voting rules, a director nominee may only be included on a proxy card if the nominee consents to such inclusion (except that, in the event of a "short-slate" contest for a minority of the board seats, the dissident is permitted to round out its proxy card with a selection of issuer nominees). As a result, shareholders voting by proxy typically receive separate proxy cards presenting competing slates; one from the issuer that lists only the issuer's nominees, and one from the dissident that lists the dissident's nominees (plus a selection of issuer nominees in the event of a "short-slate" contest). Because shareholders may only submit one proxy card under state law, they are required to choose one of the cards and, therefore, vote from only one slate. In contrast, shareholders who vote in person (which includes voting

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virtually) at a shareholder meeting are able to select nominees from a ballot that includes all of the issuer's and dissident's director nominees.

B. PREVIOUS SEC PROPOSALS FOR UNIVERSAL PROXY CARDS

The SEC has considered rules related to the use of universal proxy cards in the past. For example, in 1992, it adopted the short-slate rule, and in 2003, the SEC proposed a rule that sought to mandate the use of universal proxy cards that was never adopted. The topic regained prominence following proxy contests in recent years, and on October 26, 2016, the SEC proposed new rules mandating the use of universal proxy cards, with the comment period ending on January 9, 2017. On April 16, 2021, the SEC reopened the comment period for the 2016 proposed rules for 30 days before adopting the proposed rules at its November 17, 2021 open meeting.

OVERVIEW OF THE NEW RULE

A. INCLUSION OF NOMINEES ON PROXY CARDS

Under the new rules, in contested director elections both the issuer and the dissident must provide shareholders with a universal proxy card that lists all the nominees up for election (including the issuer's and dissident's nominees as well as any proxy access nominees). To facilitate the ability of parties to include all nominees on their proxy card, the SEC amended Rule 14a-4(d)(1)(i) to define a "bona fide nominee" as a person who has consented to being named in "a" proxy statement relating to the issuer's next shareholder meeting at which directors are to be elected (rather than "the" proxy statement of the party listing the nominee on its card). This expands the scope of a nominee's consent to include consent to being named in *any* proxy statement for the applicable meeting.

Although each party will be free to choose the design of its proxy card, the new rules set forth various presentation and formatting requirements to ensure a clear and neutral presentation of the nominees, including, among other things, requirements that the card clearly distinguish between the issuer's and dissident's nominees and that nominees must be listed alphabetically within each group, using the same font, size and style. The card must also prominently indicate the maximum number of nominees that the shareholder can cast a vote upon (regardless of how the shareholder chooses to vote for such nominees) and disclose the treatment of over-voted or under-voted cards. Finally, the new rules require that both the issuer and dissident refer shareholders to the other party's proxy statement for information about the other party's nominees.

B. NOTICE AND TIMING REQUIREMENTS

The new rules require a dissident intending to solicit proxies in support of nominees other than the issuer's nominees to provide notice to the issuer of this intention and the names of those nominees no later than 60 calendar days prior to the anniversary of the previous year's annual meeting date. The proposed notice requirement is in addition to any advance notice requirements set forth in the issuer's governing bylaws. In

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turn, the issuer is required to notify the dissident of the names of the issuer's nominees no later than 50 calendar days prior to the anniversary of the previous year's annual meeting date. Both the issuer and dissident must promptly notify the other party of any changes in its nominees. The dissident must also file its definitive proxy statement with the SEC by the later of (a) 25 calendar days prior to the meeting date or (b) five calendar days after the date the issuer files its definitive proxy statement. A failure to comply with this deadline will mean that the dissident cannot continue with its solicitation and is considered to be in violation of Rule 14a-19 (relating to false and misleading statements, and means the dissident would face the same liability as if it had violated any other proxy rules).

The SEC declined to impose a specific filing deadline for the issuer's definitive proxy statement. While in a contested election the issuer must file its preliminary proxy statement at least 10 days before its definitive proxy statement is distributed, there is no requirement for when the definitive proxy statement must be filed unless the issuer is using the "notice and access" model of delivery, in which case notice must be sent and the definitive proxy statement must be posted at least 40 calendar days before the annual meeting. Because, as a result of the sequencing of these filings, the issuer may disseminate its definitive proxy statement and universal proxy card before discovering that the dissident is not proceeding with its solicitation, the issuer's proxy statement must include disclosure advising shareholders how it will treat proxy authority granted in favor of the dissident's nominees if the dissident abandons its solicitation or fails to comply with Regulation 14A. Additionally, if there is a change in the dissident's nominees after the issuer has disseminated a universal proxy card, the issuer may, but is not required to, disseminate a new universal proxy card reflecting this change.

C. MINIMUM SOLICITATION REQUIREMENTS

The new rules require the dissident to solicit the holders of shares representing at least 67 percent of the voting power of the shares entitled to vote at the meeting. The final rule increased the minimum solicitation required from the majority of voting power which was proposed in 2016 in response to commentators' concerns that a lower threshold would result in dissidents ignoring smaller, retail shareholders and increase the potential for the "freeriding" of dissident nominees on the issuer's proxy card. The new rules do not require any solicitation cost-sharing between the issuer and the dissident. As a result, unless otherwise provided in the issuer's governing documents, the dissident will be required to pay for its own solicitation costs. The dissident may choose whether to mail the full set of proxy materials to shareholders or to use the less costly "notice and access" method. The dissident must include a statement in its nomination notice and proxy statement that it intends to satisfy this minimum solicitation requirement, and the dissident must promptly notify the company of any change in its intent to comply.

D. VOTING OPTION REQUIREMENTS

Under the new rules, proxy cards for *all* director elections (contested or not) are now required to include: (1) an "against" voting option in lieu of a "withhold authority to vote" option for elections where there is a

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legal effect to such a vote under state law; and (2) an “abstain” voting option in a director election governed by a majority (as opposed to a plurality) voting standard. The proxy statement must also disclose the treatment and effect of a “withhold” vote.

E. EXEMPT SOLICITATIONS

The new rules do not apply to solicitations in connection with director elections at registered investment companies or business development companies, solicitations that are exempt under the proxy rules or consent solicitations.

POTENTIAL IMPLICATIONS

As the SEC stated in its adopting release, it is difficult to predict the likely extent or direction that these new rules will have on proxy contests (including whether they will result in more or less proxy contests or impact the outcome of proxy contests). However, some potential implications include:

- *Voter Confusion*: Because universal proxy cards have rarely been used, shareholders who receive them may be confused about their voting choices and how to properly mark their cards. This could result in an increased submission of invalid proxies, including as a result of shareholders inadvertently voting for more nominees than there are seats available for election, or proxies that do not reflect the shareholders’ intentions. However, the presentation, formatting and procedural disclosure requirements imposed by the new rules may mitigate some of these concerns.
- *Increase in “Mixed Boards”*: By enabling split-ticket voting, universal proxy cards could lead to a greater number of boards that are composed of a mix of issuer-nominated and dissident-nominated directors.
- *Use of Other Activism Tactics*: Because the minimum solicitation requirement and other procedural requirements could increase the costs associated with launching a proxy contest, dissident shareholders may be more likely to utilize other forms of activism, such as pursuing solicitations that are exempt from the proxy rules (such as solicitations involving fewer than 10 shareholders), calling a special meeting to remove existing directors and appointing their own nominees to fill the vacancies (if permitted under the issuer’s governing documents), taking advantage of proxy access provisions and/or launching “vote no” campaigns. Issuers should review their governing documents to understand the various options available to shareholders and consider the need for any additional defenses (such as stricter advance notice bylaws or the adoption of a director qualification provision).
- *Risk of Non-Compliance*: Because the new rules impose additional deadlines and procedural requirements, issuers will need to update their proxy season checklists and work with their transfer agents and proxy solicitors to ensure they comply with all applicable requirements for affected meetings.

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